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HIRING AND USING COMPLIANCE CONSULTANTS

In the first of two recent actions involving compliance consultants, the SEC was successful in enforcing a subpoena for communications between a defendant and its compliance consultant. In the second action, the Commission rejected a firm's defense based on its reliance on its compliance consultant's advice. The authors discuss these cases and suggest takeaways for counsel to improve their chances of achieving more favorable results.

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Compliance consultants often play a critical role for broker-dealers ("BDs") and investment advisers ("IAs") by providing a firm with a particular expertise or with additional resources. While hiring an outside expert can be incredibly helpful for BDs and IAs, firms need to know what they are buying — and what they are not buying. Two recent Securities and Exchange Commission enforcement actions highlight some of those limitations. This article provides analysis based on those cases, and suggests certain ways that firms may be able to protect themselves when they do hire third-party compliance consultants.

1. Communications between a compliance consultant and a firm may be protected from disclosure to third parties, such as regulators, under certain circumstances.

In a recent SEC enforcement action, the US District Court for the District of Massachusetts needed to analyze whether an IA's communications with a compliance consultant were protected by the attorney-client privilege or the work-product doctrine. In that action, the SEC served a subpoena on the IA's securities compliance consultant requesting documents relating to the consultant's work for the IA. In response, the IA filed a motion to quash arguing that the documents and communications sought by the subpoena were privileged. To determine if the documents were protected from production to a third party, the court analyzed whether the consultant was retained to assist counsel in rendering a legal opinion and whether the consultant was hired in anticipation of litigation. Although the court ultimately denied the motion to quash,[1] the opinion provides helpful guidance about when a firm's communications with a consultant are by protected by the attorney-client privilege or work product doctrine.

The case began in early 2013, when the principal of an IA learned that FINRA brought an enforcement action against an unrelated BD for alleged misrepresentations in its marketing of exchange-traded fund ("ETF") strategies. The action resulted in a $250,000 fine. Because the principal anticipated that regulators, including the SEC, could investigate his IA for its marketing of ETF-based strategies, he engaged a

[1] *SEC v. Navellier & Associates, Inc.*, No. CV 17-11633-DJC, 2018 WL 6727057 (D. Mass. Dec. 21, 2018).

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