



Securities Industry Association

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Via Federal Express and email

April 19, 2001

Jonathan G. Katz
Secretary
Securities and Exchange Commission
450 Fifth Street N.W.
Washington, D.C. 20549

Re: Proposed Amendment to Rules under the Investment Company and
Investment Adviser Acts Regarding Electronic Recordkeeping by Investment
Companies and Investment Advisers (Release Nos. IC-24890 and IA-1932; File
No. S7-06-01)

Dear Mr. Katz:

The Investment Adviser, Investment Company and Technology and Regulation
Committees of the Securities Industry Association ("SIA")¹ are pleased to submit this comment
letter regarding certain proposed amendments to Rule 31a-2 under the Investment Company Act
of 1940 and Rule 204-2 under the Investment Advisers Act of 1940.

The proposed amendments are designed to expand the ability of mutual funds and
advisers to use electronic storage media to maintain and preserve records, consistent with the
goals of the recently enacted Electronic Signatures in Global and National Commerce Act ("esign
legislation").

The Committees generally support the proposed amendments and believe they are
consistent with the intent of the esign legislation. In particular, we applaud the fact that the
Commission has elected not to require the use of "Write once read many" ("WORM") technology
with respect to electronically stored mutual fund and adviser records as that requirement has been
an unnecessary deterrent to the broader use of electronic storage media by broker dealers.²

¹ The Securities Industry Association brings together the shared interests of more than 680 securities firms to accomplish
common goals. SIA member-firms (including investment banks, broker-dealers, and mutual fund companies) are active
in all U.S. and foreign markets and in all phases of corporate and public finance. The U.S. securities industry manages the
accounts of approximately 50-million investors directly and tens of millions of investors indirectly through corporate,
thrift, and pension plans. The industry generates in excess of \$300 billion of revenues yearly in the U.S. economy and
employs approximately 700,000 individuals. (More information about the SIA is available on its home page:
<http://www.sia.com>.)

² See Rule 17a-4n (f) 2 (ii) (A) of the Securities Exchange Act of 1934

While, we generally support the amendments, we do have concerns about the provisions regarding the production of electronic records upon Commission request. Under current requirements such records must be provided promptly, whereas under the proposed rule, records would have to be furnished within one business day. As discussed more fully below, we believe such a stringent requirement is neither appropriate or necessary, and is not consistent with other provisions of the rules related to record storage.

DISCUSSION

Storage Methodologies

First and foremost, SIA commends the Division of Investment Management on adopting an approach that favors procedural safeguards over technical ones, such as requiring WORM technology. The new rule will permit storage on any electronic media provided that the firm takes appropriate steps to (1) reasonably safeguard records from loss, alteration or destruction; (2) limit access to records to authorized personnel and regulators; and (3) reasonably ensure that any reproduction of non-electronic original records on electronic storage media is complete, true and legible when retrieved.

As the proposing release notes, “procedures to safeguard records from loss, alteration, or destruction make it possible for...the SEC to be reasonably confident that the records have not been changed in ways that cannot otherwise be detected.” Confidence in the integrity of documents is essential to the regulator’s mission. However, as the release demonstrates, this level of confidence can be achieved without imposing technical specifications on storage media.

In today’s digital world, electronic storage and retrieval is almost always “cheaper” and makes “better business sense” than the alternatives. However, the “significant benefits” cited by the release will be even more significant for those opting for electronic storage, *because* the rule omits the requirement that the storage medium be non-rewritable and non-erasable (i.e., “WORM”- compatible).

The current record storage rule applicable to broker-dealers under the Exchange Act includes the WORM requirement. When the SEC first adopted this rule in 1996, there was not an appreciable difference between WORM-compatible record storage media and non-WORM alternatives in terms of capability and performance. Today, however, WORM-compatible storage media simply cannot cope with the sheer size and number of electronic records being created by our firms.

SIA believes that the WORM requirement imposes additional costs and inefficiencies in the record keeping process and is seeking to eliminate it for broker-dealers as well.³ As the release notes, the cost of implementing a WORM record storage system outweighs the benefits.

SIA believes that such a cost-benefit analysis, which would also take account of the costs of operating and maintaining a WORM system, would be equally useful in a review of the existing rules applicable to broker dealers. For almost a year, SIA has had a constructive dialogue

³ See http://www.sia.com/key_issues/html/other_sia_initiatives.html

with staff from the Division of Market Regulation on the issue of record storage media. As part of these discussions, SIA plans to propose an alternative to the current WORM requirement and to offer evidence that would justify a change. We are encouraged by the response we have received thus far from the Division and will continue to work with them toward a resolution. In this context, we believe that the instant proposing release is very instructive in that it includes compelling arguments for a non-technical rule that make equal sense in the broker-dealer context.

The Commission should consider the proposed model for funds and advisers for all SEC-regulated entities of a broker-dealer. Integrated firms offering all of these products and services are eager to deploy technology solutions that work for the entire firm in order to leverage economies of scale. A document may be relevant for more than one reason and thus may need to be retained by more than one entity or for more than one regulator (securities or otherwise). A global approach to record storage is not only smart from a cost standpoint, but from an efficiency standpoint as well. In an increasingly consolidated industry, it does not make sense to impose separate record storage rules on different activities of the same financial institution. Section 31(a)(1) and (2) of the Investment Company Act reflects Congress' desire to minimize compliance burdens by streamlining record storage requirements for the underwriter, broker-dealer, investment adviser and investment company subsidiaries of an integrated financial institution.

We share the SEC's belief that "these proposals would allow funds and advisers greater flexibility to make (business) decisions about record keeping" and urge the SEC to grant similar flexibility to broker-dealers.

Production of Records

We urge the Commission to retain the current requirement that records, electronic or otherwise, be furnished "promptly" upon Commission request, rather than adopting a next business day requirement. We believe that the proposed change may be motivated by the belief that the technology associated with electronic storage media allows for faster retrieval of records. While this is often true, and many records can be retrieved virtually instantaneously, the time it takes to retrieve a record can vary significantly based on the form of storage medium, the age of the record, the quantity of records requested and the location of the storage facility. Thus, there is no certainty that all requested records could reasonably be produced within one business day. For example, under applicable Investment Company Act rules⁴, most required mutual fund records must be preserved for a 6-year period, the first 2 years in an "easily accessible place". In compliance with this requirement an investment company may maintain such records on optical disk and store them in a "juke box", whereby, the records can be electronically accessed from a desk top computer. After the first two years, depending on the juke box storage capacity, the disk may be removed from the juke box and stored in another location (for the remainder of the record retention period), from which it would have to be retrieved and reinstalled in a juke box or similar hardware so that the appropriate records could be obtained. In this latter instance, although the records would be stored in conformity with applicable rules, it is not clear that records could be retrieved in one business day in all cases.

Additionally, we are not aware of, nor does the Release cite instances where problems have occurred under the current production standard. Furthermore, as a practical matter

⁴ See Rule 31-2(a) under the Investment Company Act of 1940

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commission examinations usually commence with a request for production of a variety of records which are reviewed by Commission staff over a period of several days or even weeks. Thus, the need for one business day turnaround of all production requests is at best questionable, even if it were possible. Therefore, we believe that codifying a single inflexible time frame in all circumstances is unnecessary and will only lead to inadvertent violations by funds and advisers making good faith efforts to comply with Commission production requests.

We trust you will find the above comments helpful. If you have any questions concerning the content of this letter, please contact Michael Udoff (212-618-0509) or Scott Kursman (212-618-0508) of SIA staff.

Respectfully submitted,

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