Securities Industry Association
120 Broadway, New York, NY 10271-0080, (212) 608-1500, Fax (212) 608-1604
1401 Eye Street, NW, Washington, DC 20005-2225, (202) 296-9410, Fax (202) 296-9775
info@sia.com, http://www.sia.com

February 7, 1997

Jonathan G. Katz
Secretary
U.S. Securities and Exchange Commission
450 Fifth Street N.W., Stop 6-9
Washington, D.C. 20549

Re: Rules Implementing Amendments to the Investment Advisers Act of 1940,Release IA-1601, File No. S7-31-96

Dear Mr. Katz:

The Investment Adviser Committee of the Securities Industry Association ("SIA")**1** appreciates the opportunity to comment on the proposed rule amendments under the Investment Advisers Act of 1940 ("Advisers Act") to implement provisions of the Investment Advisers Supervision Coordination Act ("Coordination Act") reallocating regulatory responsibilities relating to investment advisers and investment adviser representatives between the states and the Securities and Exchange Commission ("SEC" or "Commission").

OVERVIEW

Given the very short time frame the Commission had to develop rules and interpretations to implement the provisions of the Coordination Act, the Commission has done a remarkable job of identifying issues and proposing modifications to existing rules, as necessary, in light of the requirements of the Act. The Commission has done an equally admirable job in formulating proposed rules and forms which are necessary to fulfill such requirements. Nonetheless, we believe that in certain instances alternative proposals or interpretations would better serve the Congressional intent behind the Coordination Act. We also believe that there are certain situations which are impacted by the Coordination Act that have not been addressed in the SEC Release. We will address these matters in the comments which follow.

In formulating our comments, we have been particularly mindful of the Commission's description of Congressional intent as articulated in the following passage from its release:

". . . Congress also was concerned with the cost imposed on investment advisers and their clients by overlapping, and in some cases, duplicative, regulation. In addition to the Commission, forty-six states regulate the activities of investment advisers under state investment adviser statutes. States generally have asserted jurisdiction over investment advisers that "transact business" in their state. Consequently, many large advisers operating nationally have been subject to the differing laws of manay states, Compliance with differing state laws has imposed significant regulatory burdens on these large advisers. Congress intended to reduce these burdens by subjecting large advisers to a single regulatory program administered by the Commission..."

Our comments are as follows.

FORM ADV-T DE-REGISTRATION PROCESS

We share the Staff's view that once an investment adviser has met the criteria for federal registration, the rules should be sufficiently flexible to insulate the adviser from mandated de-registration due principally to market fluctuation. We believe that the $5 million window is a step in the right direction but it should be wider. With consideration to the volatility of securities markets, we believe $10 million appears to be more reasonable. Additionally, we believe that an adviser should not be required to de-register unless it fails to meet the assets under management test (or such other formulae as the Commission may develop) for two consecutive annual filing periods. Where de-registration is nonetheless necessary, we would suggest that the grace period be 120, rather than 90 days. We believe this wider latitude is appropriate, because the de-registration process may entail a multiplicity of state registrations which would be collectively burdensome. A number of our members have commented that it s not been uncommon to be required to obtain extensions of time to complete state ADV filings, and the difficulties of meeting a 90 day requirement would only be exacerbated by the asset under management data that would have to be included in the state filing.

Also, it is our understanding from discussions with the staff that when an investment adviser files Form ADV-T to continue or initiate registration with the Commission, the Commission will send notice of such filing to the states in which the adviser has previously been registered. We believe this procedure should be mentioned in the final adopting release, since it is not addressed in the proposing release.

ASSETS UNDER MANAGEMENT

We appreciate the Commission's recognition of the fact that a large cash or cash equivalent position is a legitimate investment strategy under certain market conditions, and should not adversely impact the treatment of an account as a "securities portfolio" for purposes of its inclusion in assets under management. However, we do not believe the Commission's instruction 7(a) to Form ADV - T fully resolves the issue. Excluding cash or cash equivalents from the calculation in determining whether an account is a "securities portfolio" could still lead to exclusion of the account if the cash or cash equivalents were substantial, and the account held a reasonable, though still minority percentage of nonincludable assets, such as real estate. We believe that since cash and cash equivalents are a legitimate defense strategy and asset category in asset allocation models, they should be treated as securities as long as the account contains any other securities or has a history of owning securities.

More fundamentally, we believe that applying "assets under management" as the sole criteria (with minor exceptions) for determining eligibility for federal registration is unduly restrictive, and may compel state registration of many large advisers who do not provide the type of services which Congress intended the states to regulate. Such advisers do not engage in financial planning or direct consulting, but rather tend to provide research and market analysis on a fee basis to assist clients in making their own investment decisions.**2** Essentially, their services are of an impersonal nature, and it is interesting to note that the Commission has specifically excluded from the definition of investment adviser representatives, individuals associated with advisers, where such individuals only perform such impersonal services. Therefore, it would appear to be inconsistent to require the employers of such individuals to be state registered. We therefore respectfully suggest that such advisers be eligible for federal registration based on revenues derived from the sale of advisory services, rather than based on assets under management. An annual revenue threshold level in the $2 to $3 million range would appear to be appropriate as it is roughly equivalent to the management fees that an adviser managing $25 million in assets would generate. Alternatively, revenue derived from all sources may equally be appropriate, since we believe there are a number of investment advisers (which are also broker-dealers) that have substantial interstate opetions and significant revenues but do not have significant "assets under management." A revenue threshold level on this basis may be appropriately established in the $25 million range. This would be consistent with the Coordination Act's and the Commission's objective of making the Commission responsible for larger firms, thereby reducing these firms regulatory burdens of having to comply with differing state laws.

AFFILIATED ADVISERS

We appreciate the Commission's recognition of the fact that some firms conduct their advisory activities through separately registered advisers who are under common control, and that all should be permitted to register federally as long as any one meets eligibility criteria for federal registration. However, we do not comprehend why all affiliates should be required to have the same principal office or place of business. We do not believe that a common physical location is a necessary ingredient of common control. As firms have grown dramatically in recent years it has become quite common to operate out of more than one location. For example, a firm with its principal place of business in New York City may not only have several offices in the city, but also maintain affiliate offices across the Hudson River in New Jersey or in southern Connecticut. There is no regulatory rationale to treat such firms any differently than ones who house their affiliates under one roof. In summary, common physical locati should not be a pre-requisite to common control, and should be eliminated as a pre-condition to allowing affiliates of eligible advisers to register federally.

INVESTMENT ADVISER REPRESENTATIVE DEFINITION

We concur with the Commission's definition of the term "Investment Adviser Representative" to the extent that it excludes persons who are not directly involved in providing advice, soliciting clients, or who only give impersonal advice. This removes the prior uncertainty which existed regarding the status of support personnel who are involved in the process of formulating advice, but who do not directly provide individualized advice to clients on a regular basis. Essentially, anyone who is not in the business of dealing regularly and directly with clients should be excluded from the definition.

We also agree that registration requirements should only apply to IARs who spend a "substantial portion" on their time providing advice to retail[3] persons. However, we believe that 10% is not a reasonable yardstick for concluding that a supervised person spends a substantial portion of his or her time providing advice to natural or retail persons. As a practical matter, support personnel and others generally providing only impersonal advice, may from time to time be called upon by investment adviser representatives in their firms (or at sponsoring firms, in the case of wrap or similar programs) to assist them in explaining particular strategies or investments to retail customers. This enhances client service, and should not be discouraged by attaching registration requirements to such activity, unless done on a very frequent basis so that the distinction between direct and impersonal advice becomes blurred. We respectfully suggest that 25%, rather than 10% is a more appropriate measure of substantialness, so as to avoid inadvertently including persons, the nature of whose normal activities, the Commission has determined should not be subject to IAregistration. We also believe that similar logic dictates that accredited investors, qualified purchasers or other who are deemed to be sophisticated investors are not in need of the protections afforded by IAR registration and should be excluded from the definition of "natural" or retail persons for purposes of applying the substantialness test.

The Commission has requested comment on whether an IAR who is dually registered as a broker-dealer agent (also commonly referred to as a "registered representative") in a state, should be excepted from the definition of "investment adviser representative." We strongly support such exception, and note that several states have eliminated the dual registration requirement. Additionally, certain self-regulatory organizations already include the offering of investment advisory services in their definition of registered representative activities.**4** Furthermore, the NASD now administers a Series 66 Exam which in addition to testing knowledge of areas covered in the uniform state registered representative exam, also covers investment adviser topics. Thus the states, if they so desire, are in a position to assure themselves of the investment advisory qualifications of prospective broker-dealer agents, without requiring separate examinations or additional registrations. Broker-dealer agent licensing, in and of itself, is sufficient to confer jurisdiction on the state over all of the broker-dealer agent's activities within the state. Dual registration is one of the burdens we believe Congress intended to eliminate. It places major paperwork burdens as well as duplicative costs on broker-dealers, without providing any additional regulatory benefit to the states. Worse yet, there have been significant financial penalties imposed on broker-dealers for late registration filings, even in the absence of any substantive violation of state securities laws.

It seems that preservation of fees is a major concern of the states, as evidenced by the inclusion of Section 307 (b) in the Coordination Act. However, in light of the purposes of the Act, preservation of fees is not a reasonable basis for continuing a dual registration requirement which is redundant, burdensome and conveys no additional jurisdiction on the states. The fees issue can certainly be addressed by increasing broker-dealer agent registration fees, or in some other fashion that will not impose the burdens of dual registration.

INVESTMENT ADVISER REPRESENTATIVE/PLACE OF BUSINESS

We believe that the definition of "place of business" set forth in the proposed rules is overly broad and somewhat vague. In particular, we are unclear as to the meaning of the term "regularly provides." We would hope that the term suggests a reasonable degree of frequency, and not merely infrequent contact that might nonetheless still occur on some periodic basis. More fundamentally, we believe that to conform to Congressional intent, place of business really requires a two-tier test. First, there must be a physical location within the state from which the IAR holds himself out as "doing business, i.e. - a location where clients reasonably expect to be able to reach or meet with the IAR. Secondly the IAR must "regularly" do business from or at that location. Simply visiting a client on an occasional business trip should not suffice. This two-tiered test will help reduce the multiplicity of state registrations of IARs by large national advisers, which as noted in the Commission's Release, was a Congreional concern. Therefore, we urge the Commission to adopt the two-tier test, together with more detailed guidance as to the intended meaning of the term "regularly". Alternatively, or additionally, we urge elimination of the dual-registration requirement for IARs who are registered as broker-dealer agents. This would also largely eliminate the need for supervised persons of dual-registered firms to deal with the place of business criteria.

SUMMARY AND CONCLUSION

Based upon the foregoing, and consistent with the Congressional intent of the Coordination Act, as set forth in this letter and the Commission's Release, we recommend the following:

- Advisers de-registering with the Commission should have 120 days to complete state registrations.
- There should be an alternative (such as revenues denied from advisory services) to the "assets under management" criteria to permit certain other types of large advisers to qualify for commission registration.
- Cash and cash equivalents should be included as securities in determining whether an account qualifies as a "securities portfolio."
- Affiliated advisers under common control should not be required to have the same principal office or place of business for qualification for Commission registration.
- The appropriate measurement for meeting the "substantial portion" test for supervised persons should be 25%, rather than 10% and sophisticated investors should be excluded.
- The place of business definition should require a physical location in a state from which business is regularly done.
- An IAR that is registered as a broker-dealer agent in a state, should be exempt from dual registration.

We hope our comments are helpful, and we once again wish to compliment the staff for the thoroughness and skill of its efforts. Given the short timeframe the staff had to formulate implementing rule proposals, and the even shorter timeframe we had for comment on them, it is possible that there are implementation issues which have not been addressed. Therefore, we trust that we can continue the dialogue as new issues arise, and that the Commission will exercise its exemptive authority under the Coordination Act, as appropriate, to address such issues. We, of course, are always prepared to meet with the staff to discuss any of the matters contained in this letter, or other issues related to the implementation of the Coordination Act. In that regard, the staff should contact me at (212) 392-5531 or Mike Udoff, committee staff adviser at (212) 618-0509. Thank you.

Sincerely,

Burton M. Fendelman
Chairman
Investment Adviser Committee

cc: Barry P. Barbash, Esq.; Robert Plaze, Esq.; Stuart J. Kaswell, Esq.; Michael D. Udoff, Esq.

Footnotes

1 The Securities Industry Association brings together the shared interests of more than 760 securities firms throughout North America to accomplish common goals. SIA members -- including investment banks, broker-dealers, specialists, and mutual fund companies -- are active in all markets and in all phases of corporate and public finance. In the U.S., SIA members collectively account for approximately 90 percent, or $100 billion, of securities firms' revenues and employ about 350,000 individuals. They manage the accounts of more than 50-million investors directly and tens of millions of investors indirectly through corporate, thrift and pension plans.

2 Although such entities do not "manage money" they do fall within the definition of an investment adviser under Section 202 (a) (11) of the Investment Advisers Act.

3 The Commission's references to "natural" persons appeared to be intended to refer to retail customers in that in discussing the "substantial portion" criteria the Commission requests comment on ". . . whether the criteria for determining whether a substantial portion of an investment adviser representative's business is providing advise to ***retail*** *persons* are workable. . ."

4 See, for example, New York Stock Exchange Rule 10.