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Invested in America

January 12, 2011

Via email to rule-comments@sec.gov

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Study on Enhancing Investment Adviser Examinations

Dear Ms. Murphy:

The Securities Industry and Financial Markets Association[1] ("**SIFMA**") appreciates the opportunity to submit the following comments for the Securities and Exchange Commission's (the "**Commission**") consideration as it undertakes a study on "Enhancing Investment Adviser Examinations," as required by Section 914 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("**Dodd-Frank**").

I. Introduction

Section 914 of Dodd-Frank requires the Commission to "review and analyze the need for enhanced examination and enforcement resources for investment advisers" and to submit a report of its findings to Congress. Dodd-Frank directs the Commission to consider a number of factors, including:

- whether the Commission's efforts would be augmented and the frequency of examinations would be improved if Congress provided the Commission authority to designate a self-regulatory organization ("**SRO**") to oversee investment advisers; and

[1] SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association. For more information, visit www.sifma.org.

- current and potential approaches to examining the investment advisory activities of dually registered broker-dealers and investment advisers or affiliated broker-dealers and investment advisers.

SIFMA strongly supports the Commission taking action to enhance investor protection. As noted in our prior comment letter regarding the Commission's study under Section 913 of Dodd-Frank,[2] we believe the process of addressing investor protection concerns is a "multi-step" process. The important issues raised by Section 914 illustrate the need for a multi-step process because the issues must be addressed in conjunction with other actions contemplated by the Commission, including the development of a uniform federal fiduciary standard of care for broker-dealers and investment advisers when providing personalized investment advice about securities to retail customers.

II. Discussion

The investment advisory community includes investment advisers registered with the Commission ("**RIAs**") that primarily provide advice to sophisticated institutional clients, and independent RIAs, which in many cases are single individuals or a firm composed of a small number of individuals, that primarily provide advice to retail customers. Institutional and retail RIAs play distinct roles in the market, and their activities and business structures raise different examination and enforcement concerns. We believe a regulatory structure based on the following principles would best achieve effective and thorough examination of investment advisers without imposing new oversight costs where not necessary for improving investor protection.

- **Commission Regulation of Institutional Investment Advisers**. Investment advisers that advise institutional clients and qualified purchasers[3] are presently overseen by the Commission. Institutional firms are the primary focus of the Commission's examination efforts, and Commission oversight and examination of these firms is extensive. Subjecting firms that provide investment advice to institutions and qualified purchasers to SRO examinations and enforcement would add duplicative, and potentially inconsistent, regulatory burdens that would not augment existing Commission oversight.

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[2] SIFMA supports the development of a clearly defined, uniform federal fiduciary standard of care for broker-dealers and investment advisers when providing personalized investment advice about securities to retail customers. *See* Letter to Elizabeth M. Murphy, Securities and Exchange Commission, from Ira D. Hammerman, SIFMA (Aug. 30, 2010), *available at* http://www.sec.gov/comments/4-606/4606-2553.pdf.

[3] Generally speaking, Section 2(a)(51) of the Investment Company Act of 1940 defines a "qualified purchaser" as a natural person or entity that owns not less than $5,000,000 in investments.

- These institutional advisers often make available to independent RIAs tools and methodologies that they have developed for institutional purposes. These tools and methodologies include baseline asset allocation systems and tools for constructing portfolios. The creation of these tools and methodologies is closely linked to the development of advice for institutions and is adequately supervised by the Commission, without need for SRO oversight.

- Furthermore, the development of investment products by institutional investment advisers (for example, registered investment companies and "wrap-fee" investment programs) is currently supervised by the Commission which, in the process, has developed expertise that contributes to the oversight of these functions. The wholesale distribution of these products is integrally linked to the construction of these portfolios. Both the construction of these products and their wholesale distribution by limited purpose broker-dealers, whether or not affiliated with the institutional investment advisers creating the product, should be subject to supervision only by the Commission, which has the primary expertise regarding this product construction.

- **Protection of Retail Customers Requires Comparable Examination and Enforcement of Intermediaries.** As Section 913 of Dodd-Frank emphasizes, all intermediaries providing personalized investment advice to retail customers should be held to a comparable standard of care, whether they are RIAs or broker-dealers. An important component of holding these intermediaries to a comparable standard of care is ensuring effective oversight of these activities. Oversight of broker-dealers is bolstered by the examination and enforcement activities of SROs with respect to the broker-dealer's conduct regarding their customers and, in particular, their retail customers. Consistent with harmonizing the standard of care and regulatory oversight and supervision of broker-dealers and independent RIAs who provide personalized investment advice to retail customers, such RIAs should be subject to comparable examination and enforcement, which appears to be practically and readily achievable through use of an SRO, as discussed below.

- **An SRO Can Provide an Effective Examination Program for Independent RIAs**. RIAs that focus on providing personalized investment advice to retail customers present different concerns than do institutional advisers. Most retail RIAs that are not affiliated with a broker-dealer are small independent advisers

that, apart from their RIA status, are not otherwise subject to Commission oversight. Due to the small size of these RIAs, many do not have substantial legal and compliance departments to monitor for compliance with applicable regulatory standards. These RIAs are not regularly examined by the Commission today. An SRO with examination authority over these RIAs would be an effective supplement to the Commission's resources.

  - In light of the limited government resources available for examining and monitoring independent RIAs, including budget authorization impasses at the federal level, examination and enforcement of independent RIAs would be enhanced by an SRO. An SRO with jurisdiction over independent RIAs would be able to devote sufficient examination and, when necessary, enforcement resources to ensure investor protection standards are upheld. In addition, such an SRO would be able to focus on the specific activities and challenges that are unique to independent RIAs, thus making the SRO's efforts more effective.

- **Any SRO Examination Program Should Be Carefully Tailored to Investment Adviser Practices.** Any SRO that engages in the examinations of RIAs providing personalized investment advice to retail customers must tailor its examination program to reasonably accommodate the divergent business models and historical regulatory regimes of RIAs and their associated persons. As the Commission is well aware, the business and regulatory model for broker-dealers is very different from that of RIAs. The techniques that have been developed by existing SROs for broker-dealer activities cannot simply be applied to RIA activities. If there is to be an SRO for the examination of RIAs, there must be a fresh start in thinking about how such an examination program would work for the RIA model.

- **Duplicative Regulatory Activity Should be Avoided**. If more than one SRO is ultimately developed that could examine RIAs, business entities that have both broker-dealer and investment advisers in their corporate structure should have the option to select a single SRO to serve as their regulator for the business activity of providing personalized investment advice about securities to retail customers, but without necessarily subjecting its affiliates to regulation by that same SRO.

III. Conclusion

SIFMA supports the Commission as it undertakes to address various, interrelated investor protection concerns. By adhering to the principles outlined above, and the additional principles noted in our prior comment letters, the Commission can develop a regulatory structure that is effective and efficient in ensuring that investors are protected and are able to access the financial services they need to achieve their investment goals.

Sincerely yours,

Ira D. Hammerman
Senior Managing Director
and General Counsel

cc: Mary L. Schapiro, Chairman
Luis A. Aguilar, Commissioner
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Troy A. Paredes, Commissioner
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