October 19, 2010

Via Electronic Filing

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

Re: SEC Study on Enhancing Investment Adviser Examinations under Section 914 of the Dodd-Frank Wall Street Reform and Consumer Protection Act

Dear Ms. Murphy:

The Investment Adviser Association ("IAA")[1] greatly appreciates the opportunity to provide comments to the Commission on Section 914 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act").

Section 914 requires the Commission to "review and analyze the need for enhanced examination and enforcement resources for investment advisers." In doing so, the Commission is directed to consider: (i) the number and frequency of examinations of investment advisers by the Commission over the last five years; (ii) the extent to which having Congress authorize the Commission to designate one or more self-regulatory organizations to augment the Commission's efforts in overseeing investment advisers would improve the frequency of examinations of investment advisers; and (iii) 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. Section 914 further provides that the Commission "shall use such findings to revise its rules and regulations, as necessary" and to issue a report to Congress within 180 days, including "a discussion of regulatory or legislative steps that are recommended or that may be necessary to address concerns identified in the study."

A robust and effective examination program for the investment advisory profession is critical to the Commission's mission of protecting investors. We believe that the Commission, as an independent governmental regulator directly accountable to Congress and

[1] The IAA is a not-for-profit association that represents the interests of SEC-registered investment adviser firms. Founded in 1937, the IAA's membership consists of over 500 firms that collectively manage in excess of $9 trillion for a wide variety of individual and institutional investors, including pension plans, trusts, investment companies, endowments, foundations, and corporations. For more information, please visit our web site: www.investmentadviser.org.

the public, is the appropriate regulator for oversight of the investment advisory profession. Consistent with our longstanding position, we continue to strongly support giving the Commission the resources it needs to conduct an effective and appropriate examination and enforcement program for registered advisers.[2]

In assessing the need to enhance the investment adviser examination program, we urge the Commission to avoid equating frequency of examinations with quality of oversight. The Commission should strive to achieve an enhanced oversight program by deploying its resources wisely to identify and target misconduct and firms with high-risk characteristics, including designing and implementing "smart" examinations. While the introduction of a self-regulatory organization might result in a greater number of adviser examinations, we are not persuaded that it would result in overall improvements to the effectiveness of the current examination regime or enhanced investor protection. As noted by SEC Commissioner Luis Aguilar, an SRO "is an illusory way of dealing with the problem of resources. The issue is really one of hiring, training, and overseeing an adequate program to examine advisers."[3]

We continue to strongly oppose the creation of an SRO for investment advisers.[4] We do not believe the effectiveness of the SRO model has been demonstrated and are concerned about the lack of transparency and accountability of non-governmental regulators. The SRO model is particularly inappropriate for investment advisers, given the diverse nature of the investment advisory profession and its principles-based regulatory framework. SROs also result in unnecessary and inefficient layers of bureaucracy and cost.

Following are our comments on specific provisions of Section 914.

---

[2] We recently submitted extensive comments to the Commission on its release regarding the Section 913 study in the Dodd-Frank Act on the obligations of broker-dealers and investment advisers, including the effectiveness of SEC oversight. *See* Letter from David G. Tittsworth, Exec. Dir., IAA, to Elizabeth Murphy, Secretary, Sec. and Exch. Comm'n, re: Study Regarding Obligations of Brokers, Dealers, and Investment Advisers, Rel. No. IA-3058; File No. 4-606 (Aug. 30, 2010) ("IAA Section 913 Letter"), available on our web site under "Comments & Statements." *See also Study Regarding Obligations of Brokers, Dealers, and Investment Advisers*, SEC Rel. No. IA-3058, File No. 4-606 (July 27, 2010).

[3] Luis A. Aguilar, Comm'r, Sec. and Exch. Comm'n, *SEC's Oversight of the Adviser Industry Bolsters Investor Protection* (May 7, 2009) ("Comm'r. Aguilar Speech"). *See also* Letter from Richard H. Baker, President and CEO, Managed Funds Association, to Elizabeth Murphy, Secretary, Sec. and Exch. Comm'n, re: SEC Regulatory Initiatives Under the Dodd-Frank Act (Sept. 22, 2010) ("MFA strongly supports ensuring that the Commission has the resources it needs to fulfill its mission . . . . We are concerned that creating a new SRO for investment advisers would not result in any public policy benefit, but would create an additional layer of regulation, subjecting advisers to potentially duplicative or inconsistent requirements. We are also concerned, given the significant variation in business models among investment advisers, from small firms that advise private funds to the largest global banks that advise retail clients, that a single SRO for investment advisers would be ill-equipped to handle the diversity of issues without being cost prohibitive.")

[4] *See Capital Markets Regulatory Reform: Strengthening Investor Protection, Enhancing Oversight of Private Pools of Capital, and Creating a National Insurance Office: Hearing Before the H. Comm. on Fin. Servs*., 111th Cong. (Oct. 6, 2009) (statement of David G. Tittsworth, Exec. Dir. of the IAA) ("Tittsworth House Testimony") at 28-32.

I. Number and Frequency of Examinations

Section 914 requires the Commission to consider the number and frequency of SEC examinations of investment advisers over the last five years. The percentage of investment advisers examined ranged from 17.8% in fiscal year 2005 to 11.1% in fiscal year 2009.[5] Currently, approximately 460 examination staff and accountants are responsible for approximately 11,500 advisers (as well as approximately 7,800 investment companies).[6] In recent years, the growth in the number of investment advisers has stretched the Commission's resources.[7] The IAA has long been a strong advocate of bolstering Commission resources. Indeed, we supported self-funding provisions considered by Congress during deliberations of the Dodd-Frank legislation.

Although the final legislation does not include a self-funding provision, the Dodd-Frank Act includes provisions that will significantly increase the Commission's level of resources. For example, it doubles the level of the Commission's authorization during the next five years and allows it to establish a $100 million reserve fund.[8] These and other provisions will significantly enhance the Commission's ability to examine and inspect SEC-

---

[5] According to data derived from the Commission's annual reports, which provide percentages of advisers examined and the number of exams, as well as the annual Investment Adviser Association and National Regulatory Services *Evolution/Revolution* reports, which provide numbers of registered advisers from publicly available data, 1,530 out of approximately 8,614 registered advisers (17.8%) were examined in fiscal year 2005; 1,346 out of approximately 10,290 registered advisers (13.1%) were examined in fiscal year 2006; 1,379 out of approximately 10,446 registered advisers (13.2%) were examined in fiscal year 2007; 1,521 out of approximately 11,292 registered advisers (13.5%) were examined in fiscal year 2008; and 1,244 out of approximately 11,257 registered advisers (11.1%) were examined in fiscal year 2009. *See SEC FY2011 Congressional Justification In Brief* (Feb. 2010) ("SEC FY2011 Justification") at 20. We understand that final data from fiscal year 2010 is not yet available.

[6] *See* SEC FY2011 Justification, *supra* note 5, at 4.

[7] *See* Tittsworth House Testimony, *supra* note 4, at 27. *See also Enhancing Investor Protection and the Regulation of Securities Markets – Part II: Hearing Before the S. Comm. on Banking, Hous., and Urban Affairs*, 111th Cong. (Mar. 26, 2009) (statement of David G. Tittsworth, Exec. Dir. of the IAA) ("Tittsworth Senate Testimony") at 26-27.

[8] Section 991 of Dodd-Frank Act authorizes $1.3 billion for the Commission's budget in 2011 and increases the authorized funding level each year through 2015 to $2.25 billion. For fiscal year 2011, the Commission has requested 100 new positions for the Office of Compliance Inspections and Examinations ("OCIE"), anticipating that such staffing will enable it to conduct 50 additional examinations of advisers, 25 additional examinations of mutual funds, and 75 additional examinations of newly registered private fund advisers. *See* SEC FY2011 Justification, *supra* note 5, at 4. In addition, the Commission expects the Division of Risk, Strategy, and Financial Innovation to provide support to OCIE in its surveillance and risk-targeting efforts. *Id.* at 50. We assume that the Commission's doubling in its level of authorization over the next five years as a result of the Dodd-Frank Act will result in at least a doubling of the number of investment adviser examinations conducted. We suggest that in connection with its Section 914 study, the Commission publish information about the costs of its investment adviser examination program so that the public may evaluate the Commission's tactical deployment of resources.

registered investment advisers and provide needed resources for long-term planning and infrastructure. Moreover, the Dodd-Frank Act increases the assets under management threshold separating federally-registered and state-registered advisers from $25 million to $100 million. This will shift about 4,000 investment advisers from Commission regulation to state regulators.[9] Even considering the addition of private fund advisers, the ratio of Commission examination staff to adviser registrants will increase.[10]

Frequency of examinations is not a proxy for an effective examination and oversight program. Senator Dodd emphasized this point with respect to Section 913, stating: "in this review, the paramount issue is effectiveness. If regulatory examinations are frequent or lengthy but fail to identify significant misconduct – for example, examinations of Bernard L. Madoff Investment Securities, LLC – they waste resources and create an illusion of effective regulatory oversight that misleads the public."[11] An effective examination program focuses on preventing, detecting, and deterring fraud and other abusive practices rather than on numerical examination targets or technical violations that may not result in investor harm. We understand that it may be difficult to document situations where an effective examination program has, for example, chilled potential misconduct. In conducting this analysis, the Commission could, nonetheless, attempt to gather information about abuses and how the Commission uncovered them – whether by routine or sweep examinations, tips, complaints, referrals, or other means. The Commission could also analyze significant misconduct discovered by other regulators using various methods, as well as other qualitative measures bearing on effectiveness of oversight.

---

[9] *See, e.g.,* Investment Adviser Association and National Regulatory Services, *Evolution/Revolution 2010: A Profile of the Investment Advisory Profession* (Sept. 2010).

[10] While the number of private fund advisers that meet the registration criteria specified in the Dodd-Frank Act is currently unknown, we believe the number will be much smaller than the number of advisers shifting from SEC to state oversight.

[11] 156 Cong. Rec. S5920 (daily ed. July 15, 2010) (statement of Sen. Christopher Dodd). *See also* Financial Industry Regulatory Authority ("FINRA") Report of the 2009 Special Review Committee on FINRA's Examination Program in Light of the Stanford and Madoff Schemes (Sept. 2009) ("FINRA Report re: Stanford and Madoff Schemes"), at 5, *available at* http://www.finra.org/web/groups/corporate/@corp/documents/corporate/p120078.pdf ("FINRA examiners did come across several facts worthy of inquiry associated with the Madoff scheme that, with the benefit of hindsight, should have been pursued."); *The Madoff Investment Securities Fraud: Regulatory and Oversight Concerns and the Need for Reform: Hearing Before the S. Comm. on Banking, Hous., and Urban Affairs,* 111th Cong. (Jan. 27, 2009) (testimony of John C. Coffee, Jr., professor at Colum. Univ. Law School) (noting that Madoff's advisory activity was within the NASD's and FINRA's jurisdiction); *Enhancing Investor Protection and the Regulation of Securities Markets – Part II: Hearing before the S. Comm. on Banking, Hous., and Urban Affairs*, 111th Cong. (Mar. 26, 2009) ("[L]et me say very clearly that I don't lay the blame for the SEC's failure to respond appropriately to [Madoff]…at the feet of a lack of resources….In this instance, I am not sure we can blame resource issues.") (statement of Mary L. Schapiro, Chairman, Sec. and Exch. Comm'n during questioning).

We commend the meaningful steps recently taken by Chairman Schapiro and the Director of OCIE to enhance the effectiveness of the current oversight program of advisers and the examination staff's expertise in the securities markets.[12] OCIE has undergone significant changes and reform in the past two years, including: (1) placing a greater emphasis on fraud detection in addition to identifying potential violations of securities laws; (2) strengthening internal controls to maximize resources; (3) recruiting examiners with specialized skills; and (4) increasing examiner expertise through training.[13] Importantly, OCIE has moved aggressively to implement reforms and has focused its strategy to "identify the areas of highest risk and deploy [its] examiners against these risks, in order to improve compliance, prevent fraud, monitor risk and inform policy-making."[14] In addition to these initiatives, OCIE "plans to significantly expand and enhance its oversight of registered advisers," including improving its risk assessment and surveillance methodologies, and to devote "significant resources to conducting cause examinations arising out of tips and complaints alleging fraud or other abuse, as well as risk targeted and sweep examinations."[15]

The Division of Enforcement also has implemented significant changes. In May 2010, it launched specialized units dedicated to five areas, including asset management for hedge funds and investment advisers. The Division of Enforcement also enhanced staff training with specialized skills and implemented the Commission's newly-formed Office of Market Intelligence in January 2010, which is responsible for collection, analysis, risk-weighting, triage, referral, and monitoring hundreds of thousands of tips, complaints, and referrals received by the Commission. The Office of Market Intelligence's mission is to ensure that the Enforcement Division dedicates investigative resources to those tips, complaints, or referrals presenting the greatest threat of investor harm.[16] OCIE's referrals to Enforcement

---

[12] *See Oversight of the U.S. Securities and Exchange Commission: Evaluating Present Reforms and Future Challenges: Hearing Before the H. Sub. on Capital Markets, Insurance, and Government-Sponsored Enterprises*, 111th Cong. (July 20, 2010) (statement of Mary L. Schapiro, Chairman, Sec. and Exch. Comm'n) ("OCIE has instituted a new governance structure with an emphasis on consistency in policy, program, and deployment of risk-focused strategies to target limited resources to mission critical objectives."). *See also SEC Oversight: Current State and Agenda, Hearing Before the H. Sub. Comm. on Capital Markets, Insurance, and Government Sponsored Enterprises*, 111th Cong. (July 14, 2009) (statement of Mary L. Schapiro, Chairman, Sec. and Exch. Comm'n) and *Oversight of the SEC Inspector General's Report on the 'Investigation of the SEC's Response to Concerns Regarding Robert Allen Stanford's Alleged Ponzi Scheme' and Improving SEC Performance: Hearing Before the S. Comm. On Banking, Hous., and Urban Affairs*, 111th Cong. (Sept. 22, 2010) (testimony of Robert Khuzami, Dir. of Sec. and Exch. Comm'n Div. of Enforcement, and Carlo di Florio, Dir. of Sec. and Exch. Comm'n Office of Compliance Inspections and Examinations) ("SEC Testimony").

[13] *See Examinations by the Securities and Exchange Commission, Office of Compliance Inspections and Examinations*, (Feb. 2010) ("OCIE Examinations"), available at http://www.sec.gov/about/offices/ocie/ocieoverview.pdf.

[14] *See* SEC Testimony, *supra* note 12, at 13.

[15] *See* SEC FY2011 Justification, *supra* note 5 at 46.

[16] *See* SEC Testimony, *supra* note 12, at 7. *See also Investigating and Prosecuting Financial Fraud after the Fraud Enforcement and Recovery Act: Hearing Before the S. Comm. on Judiciary*, 111th Cong. (Sept. 22, 2010) (testimony of Robert Khuzami, Dir. of Sec. and Exch. Comm'n Div. of Enforcement) (describing recent reforms

are tracked through this system to ensure proper staff assignments, which is expected to improve the coordination between Enforcement and OCIE.[17] The Division has reiterated its focus on advisers' breach of fiduciary duty, including fraud and misleading disclosure.

We applaud these positive steps to strengthen the Commission's enforcement and examination program.[18] We also commend the Commission's adoption of Form ADV, Part 2 amendments which will provide additional information about advisers' business practices to assist in risk-targeted examinations. In addition, we recommend the Commission more regularly issue its *ComplianceAlerts* to leverage examination findings by identifying areas in which advisers should proactively focus their compliance resources.[19] We would be pleased to work with the Commission to develop additional ways to ensure a more targeted and effective examination and enforcement program for investment advisers. For example, we would welcome a dialogue between Commission staff and investment advisers about potential data that could assist the Commission in developing an enhanced oversight regime.

II. <u>Authorizing a Self-Regulatory Organization for Investment Advisers</u>

Section 914 requires the Commission to consider the extent to which having Congress authorize the Commission to designate one or more self-regulatory organizations "to augment the Commission's efforts in overseeing investment advisers would improve the frequency of examinations of investment advisers." Authorizing an SRO to inspect advisers could, of course, increase the frequency of examinations. However, we urge the Commission to resist the illusory solution of recommending an SRO for investment advisers simply to increase the number of exams to which an advisory firm is subject without considering other factors. We strongly believe the drawbacks to an SRO for advisers – which include inherent conflicts of interest, serious questions about transparency, accountability, oversight, and added costs and bureaucracy – outweigh any purported benefits. We do not believe that an additional layer of regulation and examination by a non-governmental entity will result in a more effective regulatory oversight program for advisers than enhanced Commission oversight. Thus, we continue to oppose the establishment of an SRO for investment advisers.[20]

---

and initiatives, including close collaboration with OCIE, risk-based investigations, organizational reforms, inter-agency cooperation, new Office of Market Intelligence and Dodd-Frank Act whistleblower provisions, among others).

[17] *See* SEC Testimony, *supra* note 12, at 7.

[18] We have consistently supported efforts to improve the SEC examination program for advisers. *See, e.g.*, Letter from David G. Tittsworth, Exec. Dir., IAA, to The Hon. Mary L. Schapiro, Chairman, Sec. and Exch. Comm'n, re: SEC Exams of Investment Advisers (July 29, 2009).

[19] *See* SEC, *ComplianceAlert* (Jun. 2007 and Jul. 2008). In these alerts, the Commission examination staff encourages adviser chief compliance officers to review their compliance programs for particular focus areas based on examination results, to address any compliance or supervisory weaknesses, and to implement improvements as appropriate to the firm's compliance and supervisory programs.

[20] *See* IAA Section 913 Letter, *supra* note 2; Tittsworth House Testimony, *supra* note 4, at 28-32; Tittsworth Senate Testimony, *supra* note 7, at 17-26.

We submit that the effectiveness of the SRO model has not been demonstrated either in the U.S. or abroad. Many jurisdictions do not use the SRO model and others have tested and discarded the structure over time.[21] For example, in the late 1990's, the U.K. government transferred regulatory powers from several SROs to the Financial Services Authority due to the complexities and inefficiencies of the U.K. SRO system.[22] In particular, officials stated, "[i]t has long been apparent that the regulatory structure introduced by the Financial Services Act 1986 (FSA) is not delivering the standard of supervision and investor protection that the industry and the public have a right to expect. The current two-tier system splits responsibility between the Securities and Investments Board (SIB) and the Self Regulatory Organisations (SROs), together with the Recognised Professional Bodies. This division is inefficient, confusing for investors and lacks accountability and a clear allocation of responsibilities."[23] In addition, the U.K. Treasury acknowledged that "[a] single regulator will remove the scope for duplication, gaps and inconsistency that affects the current system."[24] A U.K. government report noted the inherent conflicts of interest present in the SRO model stating that, "[t]he proliferation of regulatory bodies has been widely criticised as unnecessarily complicated, and the term 'self-regulating organisations' gave rise to the suspicion that the SROs were guarding the self-interest of their members rather than protecting the public. This suspicion was fuelled by widespread complaints about fraud, malpractice and mis-selling."[25]

---

[21] "Whereas [SROs] are rather significant in the United States, they do not play any role in the United Kingdom and are hardly of any importance in Germany. In the EU, priority is given to the statutory approach to regulation." *See* Deutsche Bundesbank, *Securities Market Regulation: International Approaches*, (Jan. 2006), *available at* http://www.bundesbank.de/download/volkswirtschaft/mba/2006/200601mba_en_securities.pdf. Similarly, Australia does not have SROs as classically defined although exchange organizations have limited self-regulatory powers. *See* Prof. Berna Collier, Comm'r, ASIC, *Ensuring Capacity, Integrity and Accountability of the Regulator* (2005), *available at* http://www.oecd.org/dataoecd/63/12/35174567.pdf.

[22] *See Enhancing Investor Protection and the Regulation of Securities Markets: Hearing Before the S. Comm. on Banking, Hous., and Urban Affairs*, 111th Cong. 35-36 (Mar. 10, 2009) (statement of Prof. John C. Coffee, Jr., Columbia Univ. Law School) ("Ultimately, the then chairman of the SIB [Securities and Investments Board], the most important of the SROs, acknowledged that self-regulation had failed in the U.K. and seemed unable to restore investor confidence."). The recent U.K. proposal to restructure the Financial Services Authority does not reinstitute the SRO model. *See* HM Treasury, A new approach to financial regulation: judgement, focus and stability, 2010, Cm. 7874, *available at* http://www.hm-treasury.gov.uk/d/consult_financial_regulation_condoc.pdf.

[23] *See* Letter from Gordon Brown, U.K. Chancellor of the Exchequer, to Sir Andrew Large, Chairman of the SIB, re: Reform of Financial Regulation (May 1997), *available at* http://www.hm-treasury.gov.uk/press_49_97.htm.

[24] *See* Press Release, U.K. HM Treasury, Plans to modernize financial regulation, Financial Services and Markets Bill published (Jul. 30, 1998), *available at* http://www.hm-treasury.gov.uk/press_126_98.htm.

[25] *See* Select Committee on Treasury, 3rd Report 1998-99, *available at* http://www.publications.parliament.uk/pa/cm199899/cmselect/cmtreasy/73/7304.htm.

There is no evidence that an SRO for advisers would be cost effective for investors or the SEC. An SRO would impose duplicative regulation as well as significant membership and other fees on investment advisers, which may be passed on to advisory clients. In addition, the SEC would still be required to expend significant resources to exercise diligent oversight of an SRO.[26] These resources would be better spent by the SEC in bolstering its own experienced staff.

The SRO model is particularly inappropriate for investment advisers. The reasons that persuaded Congress to authorize the creation of an SRO for broker-dealers in 1939 – including the high level of interconnectivity between broker-dealers as well as the highly technical issues related to settlement, execution, and reconciliation involving broker-dealer transactions – simply do not exist in the investment advisory profession. Similarly, one rationale behind the establishment of an SRO for brokers was the ability to impose ethical standards beyond those imposed by statute. In contrast, high enforceable ethical standards are already imposed on investment advisers as fiduciaries under federal law.

The activities and regulation of investment advisers vary significantly from broker-dealers. The core activity of the vast majority of SEC-registered investment advisers is providing investment advice on a discretionary basis to individual and institutional clients. The Investment Advisers Act of 1940 is a principles-based framework that contemplates oversight and enforcement by the Commission. Broker-dealer activities, on the other hand, include buying and selling securities, variable annuities, and interests in private placements; margin lending; securities lending; taking custody of client funds or securities; acting as a market maker, dealer, syndicator, underwriter, or distributor for issuers; and engaging in stock exchange floor activities. FINRA as the broker-dealer SRO takes a specific rules-based approach to its members' activities. These detailed sales practice and transactional rules are not appropriate for advisory activities governed by fiduciary principles.

Despite these differences, FINRA – a membership organization designed and developed to oversee broker-dealer activity – has indicated its desire to exercise oversight and regulation of investment advisers.[27] We oppose extending FINRA's jurisdiction to investment advisers due its lack of accountability, lack of transparency, costs,[28] track record,[29] and bias favoring the broker-dealer regulatory model.[30]

---

[26] For example, the SRO system has failed in significant respects on past occasions, requiring substantial investigation and enhanced oversight by the Commission. *See, e.g.*, SEC, Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934 Regarding NASD and the NASDAQ Market (Aug. 1996); SEC, Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934 Regarding NASDAQ as Overseen by its Parent NASD, Rel. No. 51163 (Feb. 2005).

[27] *See, e.g.*, *Capital Markets Regulatory Reform: Strengthening Investor Protection, Enhancing Oversight of Private Pools of Capital, and Creating a National Insurance Office: Hearing Before the H. Comm. on Fin. Servs*., 111th Cong. (Oct. 6, 2009).

[28] *See* FINRA, Report of the Amerivet Demand Committee of the Financial Industry Regulatory Authority, Inc. 86 (Sept. 13, 2010), *available at* http://www.finra.org/web/groups/corporate/@corp/documents/corporate/p122217.pdf (FINRA benchmarks its

The regulator for investment advisers should acknowledge and appreciate the practices, culture, regulatory structure, and broad diversity of the advisory profession.[31] FINRA's explicit advocacy of extending the broker-dealer regulatory framework to advisers makes it a particularly inappropriate choice to regulate investment advisers.[32] Instead, the SEC, with its experience, expertise and understanding of investment advisers, should continue to be the primary regulator of the investment advisory profession. As Commissioner Aguilar has stated, the Commission is "the only entity with experience overseeing investment advisers, an industry governed by the Advisers Act, which is based on a principles-based regime. By contrast, broker-dealer SROs primarily regulate through the use of very detailed, specific sets of rules and are not well versed in the oversight of principles-based regulation."[33]

Finally, we urge the Commission to ensure that its Section 914 study is not considered in a vacuum. The study should take into account other provisions of the Dodd-Frank Act relating to the Commission's oversight functions. For example, the Commission should be mindful of information that will be generated in response to Section 967, which requires the SEC to appoint an independent consultant to study whether "the SEC's oversight and reliance on self-regulatory organizations promotes efficient and effective governance for the securities markets" and "whether adjusting the SEC's reliance on self-regulatory organizations is necessary to promote more efficient and effective governance for the securities markets."[34]

---

senior management compensation based on levels in the financial services industry and states that "non-profit organizations and governmental agencies were inadequate comparables for compensation purposes").

[29] *See, e.g.*, Letter from Project on Government Oversight (POGO) to Congress calling for increased oversight of financial self-regulators (Feb. 23, 2010), *available at* http://www.pogo.org/pogo-files/letters/financial-oversight/er-fra-20100223-2.html. *See* FINRA Report re: Stanford and Madoff Schemes, *supra* note 11.

[30] While we oppose the SRO model in general for advisers, should Congress pursue such a model, we also strongly object to the notion that an existing SRO (*e.g.*, FINRA) should be the presumptive designee.

[31] There are a wide range of adviser business models, including traditional asset management firms, financial planners, wealth managers, advisers that are part of global financial institutions, small advisers with a limited number of high net worth clients, asset allocators, private fund managers, mutual fund managers, pension consultants, and others.

[32] *See* Letter from FINRA to SEC re: File Number 4-606 Study Regarding Obligations of Brokers, Dealers and Investment Advisers (Aug. 25, 2010). *See also,* Letters from FINRA to Sec. and Exch. Comm'n, re: *Certain Broker-Dealers Deemed Not to Be Investment Advisers*, Rel. No. 34-50980; File No. S7-25-99 (Feb. 11, 2005 and Apr. 4, 2005).

[33] Comm'r. Aguilar Speech, *supra* note 3.

[34] Other provisions of Dodd-Frank may implicate the structure of any effective and coordinated examination program for investment advisers. These include Section 416, which requires the General Accounting Office to conduct a study "of the feasibility of forming a self-regulatory organization to oversee private funds" and Section 919C, which requires the General Accounting Office to submit a report on "current State and Federal oversight structure and regulations for financial planners."

III. Dually-Registered and Affiliated Entities

Section 914 requires the Commission to consider 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.

If an adviser is dually registered with another regulatory agency or has an affiliate that may be regulated by another federal, state, or international regulator, the Commission should cooperate and work closely with those regulators to examine and oversee the activities of the adviser and its affiliates (*i.e.*, FINRA for dually registered advisers and broker-dealers, the Federal Reserve or other banking regulator for banking entities, the CFTC for CFTC-registered advisers, state regulators, and international regulators for global financial services companies.) In fact, Chairman Schapiro recently noted that Commission staff is "meeting regularly, both formally and informally, with other financial regulators. Staff working groups consult and coordinate with the staffs of the CFTC, Federal Reserve Board and other prudential financial regulators, as well as the Department of the Treasury, the Department of State, the Commerce Department, and the Comptroller General."[35]

Moreover, we believe OCIE's implementation of joint broker-dealer and investment adviser exams and a cross training process will result in more effective examinations of such entities.[36] OCIE staff has stated that their exams of dual registrants are coordinated and focused on understanding the interworking of the various businesses and related compliance issues, as well as research in SRO records. Furthermore, OCIE examinations that identify recurring problems or gaps in regulatory coverage are brought to the attention of other Commission divisions or offices, such as the Divisions of Trading and Markets and Investment Management.[37] We believe these significant reforms instituted at the senior levels of the Commission should be given the requisite time to produce an even more effective oversight and inspection program of these entities focused on detecting and preventing violations of the securities laws.

* * *

We appreciate the opportunity to present our views to the Commission on this important study. Please contact me, Karen L. Barr, General Counsel, or Monique Botkin, Assistant General Counsel, with any questions regarding these matters.

---

[35] *See Implementation of the Dodd-Frank Wall Street Reform and Consumer Protection Act by the U.S. Securities and Exchange Commission: Hearing Before the S. Comm. on Banking, Hous., and Urban Affairs,* 111th Cong. (Sept. 30, 2010) (testimony of Mary L. Schapiro, Chairman, Sec. and Exch. Comm'n).

[36] *See* OCIE Examinations, *supra* note 13.

[37] *Id*.

Respectfully submitted,

David G. Tittsworth
Executive Director

cc: The Honorable Mary L. Schapiro, Chairman
The Honorable Kathleen L. Casey
The Honorable Elisse B. Walter
The Honorable Luis A. Aguilar
The Honorable Troy A. Paredes

Robert W. Cook, Director
Division of Trading and Markets

Andrew J. Donohue, Director
Division of Investment Management

Henry Hu, Director
Division of Risk, Strategy, and Financial Innovation

Carlo di Florio, Director
Office of Compliance Inspections and Examinations