Business Law Section of the State Bar of Texas
Investment Funds Committee

August 7, 2018

Via Electronic Filing: rule-comments@sec.gov

Mr. Brent J. Fields
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549-1090

Re: Investment Advisers Act Release No. IA-4888 (File No. S7-08-18) Form CRS Relationship Summary; Amendments to Form ADV; Required Disclosures in Retail Communications and Restrictions on the use of Certain Names or Titles

Dear Mr. Fields:

The undersigned are members of the Investment Funds Committee (the "Committee") of the Business Law Section of the State Bar of Texas. Our practices focus on investment issues broadly, including regulatory compliance with a particular emphasis on representing managers to private funds. We appreciate the opportunity to comment on the Securities and Exchange Commission's (the "Commission") proposed Form ADV Part 3, requiring investments advisers to deliver to "retail investors" a client relationship summary ("Form CRS") disclosing certain information about the firm. We believe that Form CRS should be more tailored to disclosure to individuals that are most at risk to fail to understand the relative roles of broker-dealers and investment advisers and any disclosure made should match disclosure requirements in other client-facing forms, such as the "brochure" or "brochure supplement" in Part 2 of Form ADV.

Our more detailed responses to the Commission's request for comment on these issues are set forth below.

Definition of Retail Investor

The proposed Form ADV Part 3 would require a reporting adviser to deliver a Form CRS to any retail investor, which is defined as any prospective or existing client or customer who is an individual. We believe that this definition is overbroad and should instead be defined to exclude certain classes of individuals, consistent with previous Commission determinations. For example, statutes and other rules make distinctions about investors based on their level of net worth and investments and their presumed levels of sophistication and knowledge, including Regulation D under the Securities Act of 1933 ("accredited investor"), Section 3(c)(7) of the Investment Company Act of 1940 ("qualified purchaser") and the Investment Advisers Act of 1940 ("qualified client"). In all of these instances, the Commission acknowledged that not all individual investors require the same level of protections. We believe defining "retail investor" for the purposes of the protections of the proposed Form ADV Part 3 in line with the definition of "qualified client" under Rule 205-3 under the Advisers Act would better serve the Commission's intended purpose of protecting those individual investors who lack the sophistication and knowledge to differentiate between

broker-dealers and investment advisers and the duties of each. We note that the "qualified client" standard is an easy-to-implement threshold that can be determined through a simple questionnaire.[1]

Legal and Disciplinary Event Disclosures

The content of the Form CRS appears relatively simple and straightforward, but we have concerns about the disclosure of disciplinary issues and the mismatch with the client-facing "brochure." Item 7.B of Form CRS would require inclusion of the following statement by an investment adviser or broker-dealer: "We have legal and disciplinary events" if the broker-dealer or investment adviser, or one of its financial professionals, currently discloses or is required to disclose disciplinary information in Form ADV item 11 of Part 1A or Item 9 of Part 2A. Because the focus of ADV 1A is disclosure to the Commission, Item 11 of Part 1A functions mechanically and requires disclosure of various disciplinary history information, including many criminal, regulatory and civil judicial action if the investment adviser's actions fit within the prompt and the definition. As opposed to Part 1A, a registered investment adviser's "brochure" prepared in accordance with Part 2A of Form ADV is focused on client disclosure of the terms of service, various affiliations and conflicts of interest and material disciplinary events and is required to be distributed to clients. As opposed to Item 11, Item 9 of the brochure requires disclosure of disciplinary events that are material to the client's evaluation of the investment adviser's business or the integrity of the investment adviser's management. While the list of disciplinary items from Item 11 of Part 1A are presumed to be material, Item 9 of the brochure also provides an ability for a reporting adviser to rebut the presumption of materiality of the disciplinary event and therefore not be required to disclose it. We do not believe that an adviser that has overcome the presumption of materiality in Part 2A and properly documented it in its files should be required to disclose on proposed Form CRS that it has been subject to disciplinary events. Moreover, because detail on these legal or disciplinary events would not be required under Item 9 of Part 2A, the investor would have no further information in the brochure on these events with which to evaluate and analyze its relationship with the adviser after disclosure under Form CRS. Accordingly, we respectfully suggest the Commission limit the applicability of the Item 7.B(1) Form CRS legal and disciplinary event disclosure for registered investment advisers to only those events that the adviser has determined are material in accordance with Item 9 of Part 2A.

***

We appreciate this opportunity to provide our views on the proposed interpretation. We would be pleased to discuss our comments with the Commission or its staff at your convenience. If you would like to discuss our letter, please contact George Lee at 214-661-5524. The above does not necessarily reflect the views of the Business Law Section of the

[1] While the CRS Proposal references that Section 913 of the Dodd-Frank Wall Street Reform and Consumer Protection Act requires the Commission to conduct a study of client understanding of investment adviser and broker-dealer roles, it does not mandate the Commission to ignore wealth in adopting disclosure rules. We also note that the study cited in note 32 of the CRS Proposal does not study the sophistication of investors who satisfy the qualified client standard. *See* the CRS Proposal text at note 31.

State Bar of Texas or each member of the Committee or the firms at which our members are employed or are partners or shareholders.

Respectfully submitted,

George T. Lee
Chair

James A. Deeken
Vice-Chair