CERTIFIED FINANCIAL PLANNER BOARD OF STANDARDS, INC.

VIA ELECTRONIC MAIL

July 11, 2011

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

Re: File Number S7–17–11, Investment Adviser Performance Compensation

Dear Ms. Murphy:

Certified Financial Planner Board of Standards, Inc. (CFP Board)[1] appreciates the opportunity to comment on the rule proposed by the Securities and Exchange Commission (the Commission) to amend the qualified client standard of Rule 205-3 under the Investment Advisers Act of 1940 (Advisers Act) as required by Section 418 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act).[2] Section 418 of the Dodd-Frank Act requires the Commission to adjust for inflation the dollar amount tests (i.e., the assets-under-management test and the net worth test) in Section 205 of the Advisers Act by July 21, 2011, and every five years thereafter.[3] We support the Commission in adjusting the dollar amount tests.

Congress and the Commission have long recognized that performance fee arrangements might provide advisers with an incentive to increase advisory fees by taking undue risks with client funds.[4] Similar to approaches taken under other areas of the securities laws, the restrictions on performance fee arrangements have been relaxed to exempt an investment adviser from the prohibitions of Section 205 of the Advisers Act where a client meets certain requirements designed to serve as measures of investment sophistication and experience. Unfortunately, the dollar amount tests in Section 205 have been adjusted only one time since 1985. The inflation in asset values (and thus investor net worth) since that time has created the potential of allowing investment advisers to enter into performance fee arrangements with some clients who should not have been deemed a qualified client.[5] We are pleased with the Commission's efforts to implement Section 418 of the Dodd-Frank Act and support the

[1] CFP Board is a 501(c)(3) non-profit organization that acts in the public interest by fostering professional standards in personal financial planning through setting and enforcing education, examination, experience, and ethics standards for financial planner professionals who hold the CFP® certification. CFP Board's mission is to benefit the public by granting the CFP® certification and upholding it as the recognized standard of excellence for personal financial planning. We currently oversee nearly 63,000 CFP® professionals who agree to comply with our competency and ethics standards and subject themselves to the disciplinary oversight of CFP Board.

[2] Investment Adviser Performance Compensation, Investment Advisers Act Release No. 3198 (May 10, 2011), 76 Fed. Reg. 27,959 (May 13, 2011) (to be codified at 17 C.F.R. Pt. 275) (hereinafter Proposing Release).

[3] Pub. L. No. 11–203, 124 Stat. 1376, 1579 (2010).

[4] *See* Proposing Release, 76 Fed. Reg. at 27,960 (citing H.R. Rep. No. 2639, 76th Cong., 3d Sess. 29 (1940)).

[5] *See* Exemption to Allow Investment Advisers to Charge Fees Based Upon a Share of Capital Gains Upon or Capital Appreciation of a Client's Account, Investment Advisers Act Release No. 1731 (July 15, 1998), 63 Fed. Reg. 39,022 (July 21, 1998).

proposed adjustments to the dollar amount tests. Revising the dollar amount tests every five years to reflect the effects of inflation should help provide investors with the protections contemplated by Section 205 of the Advisers Act.

Although not required by the Dodd-Frank Act, the Commission has proposed amending the net worth test to exclude the value of the client's primary residence and the amount of debt secured by the property.[6] Any outstanding debt in excess of the market value of the residence would be considered a liability.[7] CFP Board supports the Commission's proposal to exclude the value of a client's primary residence from the net worth test. The Commission's proposal is consistent with the requirements of Section 413 of the Dodd-Frank Act, which required the value of a natural person's primary residence to be excluded from the net worth calculation for purposes of determining "accredited investor" status under Rule 501(a)(5) of Regulation D.[8] While we did not comment on the Commission's proposed rule to amend the net worth standard for accredited investors, we believe it is appropriate for the value of a person's primary residence to be excluded from the net worth tests for the qualified client and accredited investor standards in a consistent manner. Doing otherwise could result in an investor meeting the qualified client standard but not the accredited investor standard depending on the value of the investor's primary residence, a result at odds with the historic recognition of the qualified client standard being more stringent than the accredited investor standard.

We do not believe ownership of a home is necessarily indicative of investment experience or sophistication, or the ability to assume the risks associated with performance fee arrangements. An investor's primary residence is typically not a liquid asset, and the fact that an investor has equity in a home is more likely to be a function of the length of time that the investor has owned the home than the investor's experience or sophistication. Similarly, FINRA, in its recently revised Rule 2111 concerning suitability, has focused on an investor's liquidity needs (rather than gross net worth) as an important factor in evaluating securities recommendations.[9] Investment advisers, who are subject to a fiduciary duty standard that is stricter than a broker's suitability obligation, should also be subject to stricter criteria in determining that an investor is sophisticated. Therefore, investment advisers should not be permitted to consider a primary residence when evaluating whether an investor is sufficiently sophisticated for the purposes of Section 205 of the Advisers Act.[10]

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[6] Proposing Release, 76 Fed. Reg. at 27,962.
[7] *Id.*
[8] 124 Stat. at 1577–78.
[9] *See* FINRA Regulatory Notices 11-02 and 11-25.
[10] We believe that increasing the net worth threshold in Section 205 is an important and beneficial first step. However, we encourage the Commission to consider requiring investment advisers to evaluate qualitative factors in addition to net worth when determining whether an investor is sufficiently sophisticated to enter into a performance fee arrangement. As we believe the Commission has long recognized, money alone does not make an investor sophisticated or experienced.

CFP Board appreciates the opportunity to comment on the Commission's proposed rule to amend the qualified client standard of Rule 205-3 under the Advisers Act. If you should have any questions regarding this comment letter, CFP Board, the financial planners it certifies, or the CFP® marks, please contact Marilyn Mohrman-Gillis, Managing Director, Public Policy and Communications, at (202) 379-2235, or visit CFP Board's Web site at www.CFP.net.

Sincerely,

Kevin R. Keller, CAE
Chief Executive Officer