Scott C. Goebel

Senior Vice President
General Counsel
FMR Co.

MAIL: 82 DEVONSHIRE STREET V10E, BOSTON, MA 02109-3614
OFFICE: 245 SUMMER STREET, BOSTON, MA 02210
617.563.0371 FAX: 617.385.1331 SCOTT.GOEBEL@FMR.COM

October 7, 2009

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

Re: Political Contributions by Certain Investment Advisers; SEC Release IA-2910; File Number S7-18-09

Dear Ms. Murphy:

Fidelity Investments[1] appreciates the opportunity to submit comments addressing proposed Rule 206(4)-5 (the "Proposed Rule") under the Investment Advisers Act of 1940 (the "Advisers Act").[2] The Proposed Rule seeks to address the recent "pay to play" scandals involving the selection of investment advisers for public pension plans by prohibiting investment advisers, and certain other associated individuals, from making certain political contributions to government officials who have the ability to influence the selection of an investment adviser for the investments of government clients.

I. Background and Summary

Selecting an investment adviser is one of the fundamental decisions that government entities are often called upon to make. Fidelity is fortunate to have been given the opportunity to manage and administer significant government client and public pension fund assets and supports efforts to promote the highest ethical standards in the investment management industry. We believe that considerations of performance and quality services that meet the needs of investors at appropriate fee levels must be at the forefront of the investment adviser selection process of any client, including government clients.

We are concerned, however, that the Proposed Rule for investment advisers is based on the Municipal Securities Rulemaking Board ("MSRB") rules framework, which was designed to address the specific attributes of the municipal securities underwriting and dealing business. In addition, we believe that several provisions of the Proposed Rule will impose burdens on legitimate advisory business far in excess of the real risks that they are designed to address, such as the inclusion of mutual funds, the two year ban on compensation for certain violations, the look back periods for political contributions, and the excessively broad coverage of activities and individuals. As discussed in greater detail below, we believe

[1] Fidelity Investments is the largest mutual fund company in the United States and is one of the world's largest providers of financial services for 20 million individuals and institutions. Customer assets at Fidelity total more than $2.8 trillion as of June 30, 2009, including managed assets of over $1.4 trillion and an additional $1.5 trillion for which Fidelity performs recordkeeping and other administrative services. Fidelity is the nation's No. 1 provider of 401(k) retirement savings plans and a leading provider of 403(b) retirement plans for not-for-profit institutions. Fidelity provides defined contribution, defined benefit, health and welfare and stock plan services to over 16,000 employers.

[2] Political Contributions by Certain Investment Advisers, Release No. IA-2910; File No. S7-18-09 (Aug. 3, 2009) ("Proposed Rule Release").

that the Proposed Rule is overbroad, and will have a chilling effect on lawful, appropriate behavior, if adopted in its current form. We therefore ask that the Commission consider the following points[3]:

- The activities of investment advisers are significantly different from those of municipal securities underwriters and dealers, which warrants differences in regulatory approach. We suggest that the Commission use existing rules, such as the compliance program or codes of ethics rules,[4] to address pay to play abuses, rather than imposing the inapt framework of MSRB Rules G-37 and G-38 on investment advisers.

- Mutual funds should be excluded from the Proposed Rule. We note that the Commission's 1999 pay to play rule proposal[5] did not include mutual fund advisers, nor have mutual fund advisers been materially implicated in the ethical scandals the Commission seeks to address. In light of the practical difficulties of applying the Proposed Rule to mutual fund advisers and the robust regulatory framework for mutual funds, it is not clear to us why the Commission has now determined to include mutual funds in the scope of the Proposed Rule.

- Penalties for violations of the Proposed Rule, especially for first-time or inadvertent violations, should be a series of graduated sanctions instead of a two year ban on receipt of compensation. An automatic two year ban for a first offense will be unnecessarily harsh in some cases, and could cause unwarranted harm to advisory clients.

- The look back provisions for political contributions should be changed to avoid unnecessary adverse impact on the hiring and promotion practices of investment advisers.

- The Proposed Rule should apply only to individuals who have the ability and incentive to influence a government client's selection of an adviser, and only to activities that have a nexus to securing a government client's investment.

- The Commission should simplify the Proposed Rule's recordkeeping requirements; otherwise, advisers are likely to impose an outright ban on political contributions by covered personnel.

II. The Framework of MSRB Rule G-37 is Ill-Suited for Advisory Services

The Proposed Rule is modeled after MSRB Rule G-37, which bans a dealer from engaging in municipal securities business with an issuer for two years after a prohibited contribution is made to an official of that issuer. We believe that advisory relationships, whether conducted through a separate

[3] This letter reiterates many of the comments that we made in our 1999 comment letter addressing the Commission's original rule proposal. See Fidelity Investments Comment Letter on File No. S7-19-99 dated Nov. 1, 1999, available at: http://www.sec.gov/rules/proposed/s71999/locke1.htm.
[4] See Advisers Act Compliance and Procedures Rule 206(4)-7; see also Investment Company Act of 1940 Compliance Procedures and Practices of Certain Investment Companies Rule 38a-1 (collectively, "compliance program rules"). See Advisers Act Code of Ethics Rule 204A-1; see also Investment Company Act of 1940 Personal Investment Activities of Investment Company Personnel Rule17j-1 (collectively, "codes of ethics").
[5] Political Contributions by Certain Investment Advisers, Release No. IA-1812; File No. S7-19-99 (Aug. 4, 1999) ("1999 Rule Proposal").

account or mutual fund, are fundamentally different from those found in the municipal securities business. For example, the municipal securities underwriting business is conducted by broker-dealers and hence is transaction oriented, whether by specific time-limited underwritings or distribution arrangements. In contrast, investment management services provided through advisory relationships and investments in mutual funds typically involve an ongoing relationship that may last for a number of years. As another point of difference, investment management contracts with municipalities are generally awarded through a competitive bidding process that may be less prone to unethical pay to play issues, whereas underwriting contracts are more often negotiated with a particular dealer. In this context, the Proposed Rule's two year ban on receipt of compensation for committing an infraction seems ill-suited to investment management activities and may result in an overly constrained advisory relationship to the possible detriment of both client and adviser.

Approaches Based on the Compliance Program Rule or Codes of Ethics Are More Fitting. Other commenters on the Proposed Rule have proposed that existing regulatory regimes, such as the compliance program mandates of Advisers Act Rule 206(4)-7 and Investment Company Act of 1940 Act ("1940 Act") Rule 38a-1, or the codes of ethics provisions of Advisers Act Rule 204A-1 and 1940 Act Rule 17j-1, are more appropriate tools to address any pay to play issues.[6] We agree that these rules have been effective at combating many conflicts of interest issues and believe that they provide a more fitting framework for any additional guidance in the pay to play arena. We recommend that the Commission consider withdrawing the Proposed Rule, and instead develop rules using the compliance program and/or codes of ethics framework.

III. The Applicability of the Proposed Rule Should Be Narrowed to Exclude Mutual Funds

Unlike the 1999 pay to play rulemaking effort,[7] the current Rule Proposal would cover situations in which a government client invests its assets in a mutual fund, rather than only applying to private funds such as hedge funds, private equity funds or investment companies exempt from registration under the 1940 Act. The Commission's rationale for expanding the Proposed Rule to cover mutual funds appears to be based in large part on hypothetical concerns about excessive investment management fees or issues specific to the administration of college savings plans. For the reasons articulated below, we do not believe this rationale is sufficient to warrant including mutual funds in the scope of the Proposed Rule.

Little Record of Abuses with Investments in Mutual Funds. To our knowledge, almost every pay to play scandal that the Proposed Rule seeks to address occurred when an investment adviser was seeking either to manage the government client's assets directly, or when those assets were to be placed in the adviser's private fund. In fact, only one of the instances cited in the Proposed Rule concerned the improper purchase or selection of mutual funds for government clients.[8] In the ten

---

[6] See Investment Company Institute Comment Letter on File No. S7-18-09 dated Oct. 6, 2009 available at: http://www.sec.gov/comments/s7-18-09/s71809.shtml ("ICI Comment Letter"). See also Investment Adviser Association Comment Letter on File No. S7-18-09 dated Oct. 6, 2009 available at: http://www.sec.gov/comments/s7-18-09/s71809.shtml.

[7] See 1999 Rule Proposal.

[8] See Proposed Rule Release at footnote 164 (See Elliot Blair Smith, Fund Scandal Worries Tuition Plan Investors, USA TODAY (Nov. 19, 2003), at B1 (reporting that the former governor of Wisconsin received campaign contributions from the founder of a mutual fund company, and subsequently the then-governor's staff created a panel of four state employees that selected the founder's firm to manage the state's 529 plan and provide the plan's investment options)).

years since the Commission first proposed rules in this area that specifically *excluded* mutual funds, it does not appear that unethical pay to play practices have involved mutual funds to the same extent that these practices have touched direct management of a government client's assets or management through an adviser's private fund.

Existing Regime Provides Substantial Protection for Investors. The Commission suggests that pay to play activities may result in advisers charging higher advisory fees to recoup the costs of contributions used to acquire the government client business.[9] The mandates and restrictions of the 1940 Act mitigate this risk and provide substantial investor protections in any context in which mutual funds are offered, including government sponsored college savings plans. Rather than list all of the provisions of the 1940 Act that serve to protect investors, we note with favor the arguments advanced by the Investment Company Institute in this area.[10]

Practical Difficulties in Identifying Government Investors in Mutual Funds. We acknowledge that the Commission has made some accommodation to the distinctions between mutual funds and other advisory relationships, specifically by excluding a government client's investment in a mutual fund outside of a government savings program from the Proposed Rule's two year compensation ban. However, we believe that the Commission should also determine that the other provisions of the Proposed Rule should likewise not be applied to mutual funds, both for the reasons stated above and because of the significant practical difficulties that funds would face when attempting to comply with the Proposed Rule.

The Commission acknowledges that because mutual fund shares are publicly offered securities made available through a variety of distribution channels, a mutual fund's adviser often has no way of knowing its potential investors, including government clients, which the adviser may be presumed to have been "soliciting" as defined under the Proposed Rule.[11] For example, distribution arrangements are common where an adviser's mutual funds are sold through unaffiliated third-party brokerage intermediaries who independently solicit and service mutual fund business for their institutional customers, including plans and programs of government clients. Thus, if an adviser's mutual fund shares are sold by an intermediary to a government plan or program through an omnibus account, the adviser to the fund has *no knowledge* of the underlying shareholder and therefore would not be able to determine when a government client has purchased shares in order to comply with the Proposed Rule. These practical difficulties are compounded in the context of fund-of-funds and sub-advisory arrangements, as these vehicles possess additional layers of potentially unknown investors.

IV. Two year Ban Leads to Severance of an Advisory Relationship and is Unduly Costly to the Client

Imposing a two year ban on compensation is extremely likely to result in termination of the advisory relationship with a government client. Unwinding a pre-existing advisory relationship may involve considerable transaction costs to a client, and ultimately to any underlying public investors. For example, additional costs would be incurred for, among other things, new undertakings of investment due diligence and a public "request for bids" process. Further, substantial legal and administrative costs may be incurred when entering a new contract with a substitute investment

[9] See Proposed Rule Release at 59.
[10] See ICI Comment Letter.
[11] See Proposed Rule Release at 64.

adviser, and significant transaction costs may be associated with the likely transfer and liquidation of portfolio assets, particularly with regard to investments in less liquid securities. Many clients and investors also have multiple financial relationships with an adviser and that adviser's affiliates. For example, a participant in a 403(b) retirement plan may choose also to have brokerage, banking, and insurance relationships with affiliates of the adviser as a result of the benefits of having integrated services offered through connected on-line interfaces. It would be highly inconvenient and disruptive for the client and the investors to be forced to switch plan adviser and possibly plan recordkeeper in connection with its investments and financial services.

Exclude Pre-Existing Relationships. Should the Commission determine to adopt the two year ban on compensation, it should not apply the ban in circumstances where a prohibited contribution occurred after a contract for investment advisory services had been executed. As the MSRB has clarified, the G-37 ban does not apply when the contribution was made after the contract was signed; that is, it typically does not apply to pre-existing business.[12] We believe these interpretations should be considered by the Commission in adopting any form of the Proposed Rule.

Graduated Sanctions Are More Appropriate. While a two year ban on receipt of compensation may be appropriate in certain egregious instances, we do not believe that an automatic ban ought to follow from a prohibited contribution where the contribution may have been small and the violation inadvertent. For such violations we suggest that the Commission consider adopting a series of graduated sanctions that take into account all salient facts and circumstances, including whether the adviser has appropriate policies and procedures in this area.

V. The Look Back Period Is Overbroad and Potentially Constrains Qualified Employees

The look back language of the Proposed Rule may have unintended consequences with respect to an adviser seeking to maintain or improve the quality of its services, especially with regard to new hires and internal promotions. To mitigate these concerns, the Commission should revise the look back provision to exclude contributions made by individuals (1) before becoming "executive officers" or "covered associates" (2) while working for a different, unaffiliated employer; and (3) to unsuccessful candidates or to officials who were not in a position to influence the selection process at the time of the contribution. Notably, G-37 applies the two year look back only to Municipal Finance Professionals ("MFPs") who solicit municipal securities business. For supervisory MFPs, the look back period is six months. We suggest the Proposed Rule take a similar approach by imposing different look back periods based on an individual's supervisory or sales role.

VI. The Proposed Rule's Coverage Is Unduly Broad and Should Be More Narrowly Tailored

Generally, many of the Proposed Rule's key definitions concerning covered persons and activities are overly broad and the Commission should limit the Proposed Rule's application. Specifically, we suggest refining the definitions of concepts such as "solicit," "covered associate," "executive officer," "official," and "payments" and support the arguments advanced in the ICI's and Investment Advisers Association's comment letters for more precision. In addition, we also urge the Commission to clarify that typical compensation provided under mutual fund or investment advisory distribution

---

[12] See Rule G-37 Interpretation – Interpretation on the Effect of a Ban on Municipal Securities Business under Rule G-37 Arising During a Pre-Existing Engagement Related to Municipal Fund Securities, April 2, 2002,MSRB Rule Book (Jan. 2002) at 241.

arrangements with registered broker-dealers or other intermediaries are outside the scope of the prohibition around "payments."

VII. Recordkeeping Requirements Will Likely Lead to a *De Facto* Ban on Any Political Contributions by Individuals in the Asset Management Industry

The complex and extensive recordkeeping requirements of the Proposed Rule suggest to Fidelity that a large adviser may have to consider, from an administrative point of view, prohibiting all employees from making any contribution to an elected official, governmental body or any political action committee ("PAC"). To guard against this, we request that the Commission consider simplifying the recordkeeping rules to: (1) apply them on an annual rather than a continual basis, and (2) eliminate the requirement that an adviser keep records on individual employee contributions to PACs, other than those controlled by the adviser. The degree of intrusion upon an employee's personal political activities, which may cover PACs dedicated to sensitive topics, does not further the goals of the Proposed Rule. As an alternative method of compliance, we request that the Commission consider permitting advisers to obtain certifications from covered associates that the associates have no knowledge of contributions to political parties that are earmarked or known to be provided for the benefit of a particular political official.

* * * * *

We would like to thank the Commission for considering our comments. Please contact me at (617) 563-0371 should you have any questions regarding this letter.

Sincerely yours,

Scott C. Goebel

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

Andrew J. Donohue, Director, Division of Investment Management