

November 2, 2007

Via Electronic Filing

Nancy M. Morris
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

Re: Interpretive Rule under the Advisers Act Affecting Broker-Dealers, Rel. No. IA-2652, File No. S7-22-07

Dear Ms. Morris:

The Investment Adviser Association¹ appreciates the opportunity to submit comments on a proposed interpretive rule that would address the application of the Investment Advisers Act of 1940 to certain activities of broker-dealers.² The proposal would reinstate three interpretive provisions of the Commission's rulemaking relating to the broker-dealer exception under the Advisers Act, which was invalidated by the D.C. Circuit Court of Appeals earlier this year.³ The IAA supports the Commission's reinstatement of these interpretive positions, with comments and modifications with respect to certain aspects of the proposal as discussed below. In addition, we re-emphasize below our previous comments related to investor education and the RAND study.⁴

¹ The Investment Adviser Association (formerly the Investment Counsel Association of America) is a not-for-profit association that represents the interests of SEC-registered investment adviser firms. Founded in 1937, the Association's current membership consists of about 500 firms that collectively manage in excess of \$8 trillion in assets for a wide variety of individual and institutional clients. For more information, please visit our web site: www.investmentadviser.org.

² *Interpretive Rule Under the Advisers Act Affecting Broker-Dealers*, Rel. No. IA-2652 (Sept. 24, 2007) (Proposal).

³ See *Financial Planning Association v. S.E.C.*, 2007 WL 935733, C.A.D.C. (Mar. 30, 2007) (vacating Advisers Act rule 202(a)(11)-1 adopted in *Certain Broker-Dealers Deemed Not To Be Investment Advisers*, SEC Rel. Nos. IA-2376; 34-51523; File No. S7-25-99 (Apr. 12, 2005) ("Final Rule")).

⁴ When the Commission approved the Final Rule in April 2005, it also directed Commission staff to report on "any rulemaking action that the staff would be prepared to recommend that the Commission undertake in the near term," as well as options and recommendations for a study "to compare the levels of protection afforded retail customers of financial service providers under the Securities Exchange Act and the Investment Advisers Act..." In June 2006, the Commission issued a Request for Information for "a study that will involve collecting, categorizing and analyzing empirical data regarding the marketing, sale, and delivery of financial products, accounts, programs and services offered to individual investors by broker-dealers and investment advisers."

Discretionary Management

The IAA has been actively involved in this rulemaking since its inception in 1999. Throughout the debate involving this rule, the IAA has consistently taken the position that discretionary investment management cannot be deemed to be “solely incidental” to brokerage services.⁵ We commended the Commission for the aspect of the rule it adopted in 2005 confirming that discretionary advice provided on a commission basis is not “solely incidental” to brokerage services.⁶ In response to the court’s ruling, we, along with other groups, urged the Commission to: (i) provide guidance to brokers on their obligations, given the court’s decision, and information to investors about implications of the court decision while a more permanent policy is being developed; and (ii) reaffirm pro-investor aspects of the rule that were not overturned by the court, including the position that discretionary management services are not solely incidental to brokerage services.⁷ Accordingly, we strongly support the proposed interpretive rule confirming that discretionary investment advice is not solely incidental to the business of a broker-dealer, regardless of the form of compensation charged.

We continue to be concerned, however, with the Commission’s exception from this interpretation for situations where the broker has discretion over an account during a client’s vacation or other limited period of time.⁸ Discretionary management over an account “for a few months” should not be deemed to be an activity that is solely incidental to brokerage services. Further, as we discussed in our 2005 comment letter,⁹ a client’s decision to grant such authority to a broker even for a limited period is indicative of the type of relationship of

Request for Information/Draft Solicitation, SEC Rel. No. 34-54077 (June 30, 2006). In September 2006, the Commission awarded the contract to RAND to conduct this study. See Press Release, “SEC Awards Contract for Study to Compare Roles of Investment Advisers, Broker-Dealers,” Rel. No. 2006-162 (Sept. 26, 2006).

⁵ See, e.g., Letter from David G. Tittsworth, Investment Counsel Association of America, to Jonathan G. Katz, Secretary, SEC (Jan. 12, 2000); Letter from David G. Tittsworth, Investment Counsel Association of America, to Jonathan G. Katz, Secretary, SEC (Feb. 7, 2005) (“Feb. 7, 2005 Letter”).

⁶ See Final Rule.

⁷ See Letter from David G. Tittsworth, Investment Adviser Association, Consumer Federation of America, Financial Planning Association, Fund Democracy, National Association of Personal Financial Advisors, and North American Securities Administrators Association, to the Honorable Christopher Cox, Chairman, SEC (Apr. 24, 2007). We incorporate that letter by reference here. See also Letter from Karen L. Barr, Investment Adviser Association, to Andrew J. Donohue, Director, SEC Division of Investment Management (July 3, 2007) (“It is important that the Commission retain investor protections in whatever rulemaking or interpretation will be provided in response to the court’s ruling”).

⁸ Proposal at n.13 (stating the Commission’s view that it would consider discretion to be temporary or limited under seven circumstances, including when the broker is given discretion “on an isolated or infrequent basis, to purchase or sell a security or type of security when a customer is unavailable for a limited period of time not to exceed a few months”).

⁹ Feb. 7, 2005 Letter, *supra* n.5.

trust and confidence that may confer a fiduciary duty on the broker.¹⁰ Such clients should be accorded the fiduciary protections of the Advisers Act.

In addition, the proposed rule language pertaining to this interpretation appears less precise than it was in the vacated rule. Accordingly, we respectfully suggest the following modification to the proposed rule text in subsection (a)(2): “Exercises investment discretion (as that term is defined in section 3(a)(35) of the Securities Exchange Act of 1934 (“Exchange Act”) (15 U.S. C. 78c(a)(35)) *with respect to any account*, except investment discretion granted by a customer *only* on a temporary or limited basis over such account.” (*emphasis added on proposed modifications*).¹¹

Investor Education and Protection

As we stated in previous correspondence to the Commission, we believe the Commission can and should play a much more proactive role in educating investors and consumers about the fundamental issues involved in this rulemaking.¹² The Commission’s Office of Investor Education and Advocacy, for example, should take a leading role in developing and providing educational information to the public about the confusion that arises when broker-dealers provide investment advice to their customers. As the Commission’s own focus groups have revealed, investors are “generally confused about the distinctions between brokers, financial advisors/consultants, investment advisers and financial planners.”¹³ Accordingly, we recommend that the Commission take this opportunity to inform investors and the public about the differences between brokerage and advisory activities, the laws and regulations governing each, and specific issues raised by this and the principal trade rulemakings. We strongly believe the Commission must play a central role in educating the investing public about these important issues and we stand ready to assist the Commission in any way that may be helpful.¹⁴

In addition, Chairman Cox has announced that the RAND study of the marketing, sale, and delivery of financial products and services to investors in this area will be accelerated so

¹⁰ See Final Rule at n.98 and accompanying text.

¹¹ Consistent with our comments above, this proposed language is submitted subject to modification of the SEC’s proposed interpretation of “temporary or limited basis.”

¹² Letter from David G. Tittsworth, Investment Adviser Association, to the Honorable William H. Donaldson, Chairman, SEC (June 22, 2005).

¹³ *Results of Investor Focus Group Interviews About Proposed Brokerage Account Disclosure*, SEC (Mar. 10, 2005), at 8.

¹⁴ Last year, for example, we worked with state regulators, consumer groups and others in publishing an investor education brochure called “Cutting through the Confusion.” After a meeting with the Office of Investor Education in October 2006, various links to the brochure were included on the Commission’s web site. Linking the brochure on the web site was a positive first step in educating investors. Unfortunately, the links to this investor education piece have recently been removed. Reinstating references to the educational brochure would assist in providing helpful information to investors about issues they confront when engaging the services of an investment professional.

that it is delivered to the Commission no later than December 2007.¹⁵ He noted that the results of the study are expected to provide an “important empirical foundation for considering improvements” in this regulatory area.¹⁶

We have previously outlined some of our concerns related to the proposed study.¹⁷ We believe it is crucial for the Commission to focus its resources on clarifying the distinctions between advisers, brokers and planners, on educating investors about these distinctions, and on protecting investors by enforcing the law in these areas. We would welcome the opportunity to work with the Commission and its staff in connection with future rulemaking in this area or evaluation of the RAND study and any ensuing Commission action related to these important issues.

Sincerely,



Karen L. Barr
General Counsel

cc: Hon. Christopher Cox
Hon. Paul S. Atkins
Hon. Annette L. Nazareth
Hon. Kathleen L. Casey

Andrew J. Donohue, Director, Division of Investment Management
Robert E. Plaze, Associate Director, Division of Investment Management

¹⁵ See Press Release, “Commission Seeks Time for Investors and Brokers to Respond to Court Decision on Fee-Based Accounts,” Rel. No. 2007-95 (May 14, 2007) (“2007 Press Release”).

¹⁶ 2007 Press Release.

¹⁷ See n.12, *supra*.