

August 4, 2005

Via Electronic Filing

Mr. Jonathan G. Katz
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-9303

Re: Petition for Rulemaking; Request for Extension of Certain Compliance Dates filed by the Securities Industry Association relating to Investment Advisers Act Rule 202(a)(11)-1

Dear Mr. Katz:

The Investment Adviser Association¹ is writing to express its strong opposition to the request by the Securities Industry Association² to extend certain compliance dates for the rule adopted by the Commission earlier this year relating to the broker-dealer exception under the Investment Advisers Act.³

Specifically, we oppose the SIA's request to delay implementation of the aspect of the rule that requires brokerage firms to treat accounts as investment advisory accounts if the broker exercises investment discretion on more than a "temporary or limited" basis.⁴

¹ The Investment Adviser Association is a not-for-profit association that represents the interests of SEC-registered investment adviser firms. Founded in 1937, the IAA's membership today consists of more than 400 firms that collectively manage in excess of \$5 trillion. For more information, please visit our web site: www.investmentadviser.org.

² Letter from Ira D. Hammerman, Securities Industry Association, to Jonathan G. Katz, Securities and Exchange Commission (July 28, 2005). The SIA letter also requests an extension of time based upon provisions of the rule relating to financial planning. A similar request has been made by the American Council of Life Insurers. See Letter from Carl B. Wilkerson, American Council of Life Insurers to Jonathan G. Katz, Securities and Exchange Commission (July 27, 2005).

³ See *Certain Broker-Dealers Deemed Not To Be Investment Advisers*, Release Nos. IA 2376; 34-51523; File No. S7-25-99 (April 12, 2005).

⁴ The rule provides that a broker-dealer will not be deemed to be an investment adviser based solely on its receipt of special compensation, provided that "[a]ny investment advice provided by the broker or dealer with respect to accounts from which it receives special compensation is solely incidental to the brokerage services provided to those accounts (including, in particular, that the broker or dealer does not exercise investment discretion as provided in paragraphs (b)(3) and (d) of this section)..." 17 CFR §275.202(a)(11)-1(a)(1)(i). Paragraph (b)(3) provides: "A broker or dealer provides advice that is not solely incidental to the conduct of its business as a broker or dealer within the meaning of section 202(a)(11)(C) of the Advisers Act or to the brokerage services provided to accounts from which it receives

Our opposition to the SIA’s request is based on several considerations: (1) the determination of whether a broker-dealer exercises investment discretion is not difficult or time-consuming and therefore an extension of time is unwarranted; (2) in its previous comment letter, the SIA requested the Commission to modify the final rule to include the “temporary or limited” provisions but never indicated that making such a determination was difficult or time-consuming and, therefore, it is unfair to further delay implementation of this rule based on inclusion of this provision in the final rule; (3) the SIA and its members have been aware for several years of the inevitability that the final rule would require brokers to treat discretionary accounts as advisory accounts; and (4) the rule already has been delayed for several years and acceding to the SIA’s request will further delay efforts to inform investors about differences between brokerage and advisory accounts and thus will not serve the Commission’s mission of protecting investors.

- 1. The determination of whether a broker-dealer exercises investment discretion is not difficult or time-consuming and therefore an extension of time is unwarranted.** The final rule in relevant part states that a broker-dealer provides advice that is not solely incidental to its primary business if the broker-dealer provides “investment discretion” over the account. In turn, the term “investment discretion” is referenced to section 3(a)(35) of the Securities Exchange Act – the primary law governing the conduct and activities of broker-dealers. The definition of investment discretion is not a new term for broker-dealers and there is no evidence that making a determination of whether a broker-dealer exercises investment discretion is a difficult or time-consuming activity. In numerous previous comment letters related to this proceeding, the SIA and its member firms did not request a lengthy implementation period in order to make such a determination.
- 2. In its previous comment letter, the SIA requested the Commission to modify the final rule to include the “temporary or limited” provisions but never indicated that making such a determination was difficult or time-consuming and, therefore, it is unfair to further delay implementation of this rule based on inclusion of this provision in the final rule.** In its most recent comment letter to the Commission,⁵ the SIA argued that the definition of “investment discretion” set forth in the Securities Exchange Act is “too broad” for purposes of the rulemaking and that the Commission should

special compensation within the meaning of paragraph (a)(1)(i) of this section if the broker or dealer (among other things, and without limitation):... (3) Exercises investment discretion, as that term is defined in paragraph (d) of this section, over any customer accounts.” Paragraph (d) provides: “For purpose of this section, the term investment discretion has the same meaning as given in section 3(a)(35) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(35)), except that it does not include investment discretion granted by a customer on a temporary or limited basis.”

⁵ Letter from Ira D. Hammerman, Securities Industry Association to Jonathan G. Katz, Securities and Exchange Commission (February 7, 2005).

modify the rule to recognize “discretion limited by customer instructions” in certain circumstances.⁶ However, the SIA certainly did not argue that such a determination is either difficult or time-consuming and did not request a lengthy implementation period in order to accommodate such a provision. In response to the request by SIA (and others), the final rule permits broker-dealers to exercise investment discretion on a temporary or limited basis without having to treat such accounts as advisory accounts.⁷ Having requested this special accommodation in the rule, we believe it is a bit disingenuous to now argue that determining compliance with this provision will involve “a labor-intensive and time-consuming process.”⁸ If complying with this aspect of the rule requires such an extraordinary effort by its members, the SIA certainly should have informed the Commission at the time it was asking the Commission to include such a provision in the final rule.

- 3. The SIA and its members have been aware for several years of the inevitability that the final rule would require brokers to treat discretionary accounts as advisory accounts.** The SIA has been an active participant in this proceeding during the 5½ years this rulemaking has been pending. In fact, the SIA and some of its members were actively engaged in requesting the Commission to initiate such a rulemaking in 1999. While the rule has gone through various changes during its lengthy history, the central rationale for the rule has remained unchanged, *i.e.*, imposing fees (instead of commissions) should not automatically “convert” brokerage accounts into advisory accounts. And the primary mechanism for achieving this result – and to create a bright line test between brokerage and advisory accounts – is to focus on whether a broker-dealer exercises “investment discretion” over the account. The SIA consistently has supported the central rationale for the rule⁹ and has never argued that a lengthy implementation period will be required to effect such a result. Now, more than three months after the final rule was adopted by a unanimous vote of the Commission, the SIA has – for the first time – indicated that at least a year will be needed to effectuate the rule’s provisions. As noted above, we do not believe that making the determination

⁶ *Id.*, at 17. “We recommend that the Commission, while continuing to provide investors with the benefits and choices afforded by limited discretionary accounts, modify the Rule so as to provide that broker-dealers’ having discretion limited by written customer instructions as to: (1) time periods of a temporary nature; (2) one or more specific securities or types of securities; or (3) prices at which they can be purchased and, in some cases, sales can be made, are not exercising discretionary investment advice.”

⁷ *Supra* n. 3 at 64-65. “Therefore, the final rule permits broker-dealers to exercise investment discretion on a temporary or limited basis without becoming ineligible for the exception under the rule. In such cases, the customer is granting discretion primarily for execution purposes and is not seeking to obtain discretionary supervisory services. Such discretion must be limited to a transaction or series of transactions and not extend to setting investment objectives or policies for the customer.”

⁸ *Supra* n. 2 at 3.

⁹ *Supra* n. 5 at 3. “SIA strongly believes that the central position reflected in the Rule is beneficial to broker-dealer customers.”

of “investment discretion” (and, in certain cases, whether the customer has granted the broker-dealer discretion on a “temporary or limited” basis) is difficult, time-consuming, or burdensome. Having made the decision to provide discretionary investment services (and many brokerage firms having done so before the final rule was adopted), we believe it is reasonable, fair, and appropriate to ask broker-dealers to comply with the rule within the six-month time frame specified by the rule.

- 4. The rule already has been delayed for several years and acceding to the SIA’s request will further delay efforts to inform investors about differences between brokerage and advisory accounts and thus will not serve the Commission’s mission of protecting investors.** While there are major differences among the various interests that have participated in this rulemaking, no one disputes the proposition that this rule has important consequences in terms of investor protection – including the prominent statement that must accompany advertisements, agreements, and other forms relating to brokerage accounts that receive special compensation. Following the Commission’s unanimous vote on April 6 approving the new rule, the SIA issued a press release calling the rule a “victory for investors” and stating that the SEC “made the right decision.” The press release touted the alleged virtues of fee-based brokerage accounts and noted that the SIA had led the victorious fight resulting in the Commission’s action to make the former “no-action” position permanent, arguing that many brokers would “stop offering fee-based accounts rather than be subject to such a burdensome and redundant regulatory arrangement.”¹⁰ More than three months later, the SIA obviously is now balking at actually following through with the changes that the rule entails. Despite praising the Commission’s adoption of the new rule, it is abundantly apparent that the SIA and its members are seeking to delay any rule that requires brokers to treat accounts as advisory accounts, whatever the circumstances.¹¹ In fulfilling its fundamental mission to protect investors, we believe the Commission should deny the SIA’s request to extend the compliance date and should seek to enforce the rule as adopted.

We also take this opportunity to reiterate the concerns we expressed in our recent letter related to this important rulemaking.¹² First, we urge the Commission to dedicate adequate resources to ensure that the rule is properly implemented and that broker-dealers comply fully with its requirements. Second, we urge the Commission to take a proactive role in educating investors and consumers about the fundamental issues involved in this

¹⁰ Press release, Securities Industry Association (April 6, 2005).

¹¹ The SIA letter states: “The SIA believes an extension would be consistent with the need for a study, and would provide the Commission time to determine the most prudent course in response thereto.” Evidently, the SIA hopes to delay this proceeding in hopes that the proposed Commission study will lead to a reconsideration of the aspects of the final rule the SIA dislikes.

¹² Letter from David G. Pittsworth, Investment Adviser Association to The Honorable William H. Donaldson (June 22, 2005).

rulemaking. After more than five years since the rulemaking was initiated, we believe it is time for the Commission to move forward to implement and enforce the rule it has adopted and to educate investors and the public about these issues.

As always, we appreciate the opportunity to provide our views on this important subject and we stand ready to assist the Commission and its staff in any manner. Please do not hesitate to contact us if you have any questions or need any additional information.

Sincerely,

A handwritten signature in dark ink that reads "David G. Tittsworth". The signature is written in a cursive style with a prominent initial "D".

DAVID G. TITTSWORTH
Executive Director

Cc: The Honorable Christopher Cox
The Honorable Cynthia A. Glassman
The Honorable Paul S. Atkins
The Honorable Roel C. Campos
The Honorable Annette Nazareth
Mr. Giovanni Prezioso
Mr. Meyer Eisenberg
Mr. Robert L.D. Colby
Mr. Robert E. Plaze