

MEMO# 22489

May 5, 2008

ICI Draft Comment Letter on the SEC's Proposed Amendments to Part 2 of Form ADV

[22489]

May 5, 2008

TO: COMPLIANCE ADVISORY COMMITTEE No. 8-08
INVESTMENT ADVISERS COMMITTEE No. 9-08
SEC RULES COMMITTEE No. 34-08
SMALL FUNDS COMMITTEE No. 16-08 RE: ICI DRAFT COMMENT LETTER ON THE SEC'S
PROPOSED AMENDMENTS TO PART 2 OF FORM ADV

As we previously informed you, [\[1\]](#) the Securities and Exchange Commission recently published for comment proposed amendments to Part 2 of Form ADV, the investment adviser registration form. [\[2\]](#) The proposed amendments would replace the current “check-the-box” format and related disclosure schedules with a plain English, narrative brochure that describes the business practices, conflicts of interest, and background of investment advisers and their advisory personnel. Brochures would be electronically filed through the Investment Adviser Registration Depository and made available to the public through the Commission’s website. The proposal incorporates comments the Commission received, including many from the Institute, [\[3\]](#) on the amendments to Part 2 originally proposed in April 2000 but never approved.

Comments on the proposal are due to the Commission by May 16, 2008. Please provide your comments on the Institute’s draft letter to the undersigned no later than Monday, May 12. Comments may be provided by phone (202-371-5410), fax (202-326-5839), or email (jheinrichs@ici.org).

The Institute's draft letter supports the proposed amendments to Part 2 of Form ADV and related rules under the Advisers Act of 1940; however, the letter notes that in several areas the proposed amendments would require overly detailed and technical information that is inconsistent with the Commission's goal of promoting the delivery of clear, concise, and more easily understandable disclosure. To further improve the quality and usefulness of this disclosure to investors, the draft letter recommends various revisions to certain of the items in the Form. These recommendations are as follows:

ADV Part 2A: The Firm Brochure

- Item 9: Disciplinary Information. The letter urges the Commission to focus its disclosure requirements on administrative, civil, or criminal proceedings that result in regulatory sanctions rather than disclosure involving arbitration awards, settlements, or claims.
- Item 11: Codes of Ethics, Participation or Interest in Client Transactions, and Personal Trading. The letter recommends that Form ADV, generally, and proposed Item 11, specifically, require disclosure only of such activities that involve a material conflict of interest. If an adviser has in place policies and procedures reasonably designed to minimize or eliminate those conflicts, we further recommend the Form ADV instructions allow the adviser to take the position that there is no material conflict of interest and that disclosure about the underlying practice is not required.

Attachment

- Item 12: Brokerage Practices. The letter expresses concern that the negative connotations of some of the disclosure of proposed Item 12 could lead a client to conclude that soft dollar arrangements are harmful, and therefore, adverse to the client's interest. As a result, it opposes requiring advisers who receive soft dollar benefits to disclose (i) that they have an incentive to select certain broker-dealers based on the adviser's interest in receiving those benefits, rather than on the client's interest in receiving the best execution services at the lowest available rates; and (ii) whether the adviser seeks to allocate the benefits to client accounts proportionately to the brokerage credits those accounts generate.
- Item 15: Custody. The letter recommends that proposed Item 15 be revised to require an adviser to explain the protections it has in place for safeguarding client assets rather than the negative connotations of the proposed disclosure. The letter also recommends that the Commission revise this item to clarify that disclosure is not required when the adviser's custody arrangements qualify under any of the exceptions in Rule 206(4)-2 under the Advisers Act.
- Item 17: Voting Client Securities. The letter recommends the Commission eliminate the proposed disclosure concerning how an adviser selects a third-party proxy voting service or how an adviser pays for the third party's services. Instead, it recommends that proposed Item 17.A. require only disclosure about the adviser's proxy voting policies and procedures and those of any third-party proxy voting service that the adviser retains of its own election to provide advice about proxy voting.
- Item 19: Index. The letter recommends that inasmuch as each brochure is required by proposed Item 3 to include a table of contents, proposed Item 19 be eliminated.

- Annual Delivery Requirement. The letter urges the Commission to consider an alternative approach that would require advisers to deliver their current brochures (along with a summary of material changes as proposed under Item 2) to clients only in those years when the annual update contains material changes.

ADV Part 2B: The Brochure Supplement

- Item 3: Disciplinary Information. The letter suggests that the lack of uniformity in the disciplinary disclosures that would be required under proposed Item 3 and either Rule 206(4)-4 under the Advisers Act or Form U-4 (which requires disclosure of a broker-dealer's or investment adviser's representative's disciplinary history) would only complicate compliance with the new disclosure requirements. In as much as the disciplinary information required by Form U-4 has been determined by federal and state regulators as a necessary aspect of an investment advisory representative's registration application, we encourage the Commission to reconcile the requirements of proposed Item 3 with Form U-4.
- Delivery Exceptions: The letter recommends that the Commission extend the exclusion from supplement delivery to all clients who are "qualified clients" as defined under Rule 205-3(d)(1) under the Advisers Act.

Jane G. Heinrichs
Associate Counsel

[Attachment](#)

endnotes

[1] See Memorandum to Compliance Advisory Committee No. 6-08, Investment Advisers Committee No. 4-08, SEC Rules Committee No. 22-08, and Small Funds Committee No. 9-08, dated March 14, 2008 [22342].

[2] See Amendments to Form ADV, SEC Release Nos. IA-2711 and 34-57419 (March 3, 2008), 73 Fed. Reg. 13958 (March 14, 2008) ("Release"), available on the SEC's website at <http://sec.gov/rules/proposed/2008/ia-2711.pdf>.

[3] See Memorandum to Investment Adviser Associate Members No. 17-00 and Investment Adviser Members No. 18-00, dated June 14, 2000 [11945].

Copyright © by the Investment Company Institute. All rights reserved. Information may be abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice.