

MEMO# 1420

September 26, 1989

DRAFT LEGISLATION CONCERNING PRIVATE RIGHTS OF ACTION AND ADDITIONAL ADVISER DISCLOSURES TO CLIENTS

September 26, 1989 TO: INVESTMENT ADVISERS COMMITTEE NO. 40-89 RE: DRAFT LEGISLATION CONCERNING PRIVATE RIGHTS OF ACTION AND ADDITIONAL ADVISER DISCLOSURES TO CLIENTS

Representative Rich Boucher (D-Virginia) has prepared draft legislation that would permit a private right of action under the Investment Advisers Act of 1940, would expressly require investment advisers to make only suitable recommendations to its clients, and would increase disclosure requirements by investment advisers to their customers. A copy of the draft legislation, which has not been introduced, is attached. Section 2 of the draft legislation would amend the Advisers Act to provide that any registered investment adviser (or adviser required to be registered) which violates Section 206(1) or (2) (the general antifraud provisions) or Section 208(e) (a new section that would include disclosure provisions as defined in Section 3 of the draft legislation) would be liable to any person injured by the violation. The draft legislation would also make a controlling person liable unless he (1) did not or would not have known of the violation or (2) acted in good faith and did not cause the violation (both defenses are in the draft legislation as alternatives). The statute of limitations would be three years from the violation or two years from the discovery of the violation, whichever ever occurs first. Finally, the private right of action would be in addition to any other remedy available and could not be waived through a dispute arbitration clause. The draft legislation also would prohibit all investment advisers from: (1) making unsuitable recommendations; (2) failing to disclose conflicts of interest; (3) failing to disclose a total fee and commission cost for any contract for services; (4) failing to disclose specific non-cash compensation amounts; (5) making any misrepresentations or omitting material facts concerning the adviser's qualifications, services or fees; (6) providing a third party recommendation or report without disclosing that fact; or (7) guaranteeing a client a specific result will be achieved. This draft legislation will be a major discussion item at the Investment Advisers Committee meeting on October 10, 1989. Your input on this draft legislation at the meeting will be appreciated. Robert L. Bunnell, Jr. Assistant General Counsel Attachment

should not be considered a substitute for, legal advice.