

**MEMO# 18969**

June 22, 2005

# **NEW YORK BAR SUBMITS RULEMAKING PETITION TO SEC REGARDING RETENTION AND PRODUCTION OF E-MAIL BY INVESTMENT ADVISERS**

©2005 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. [18969] June 22, 2005 TO: COMPLIANCE ADVISORY COMMITTEE No. 45-05 CHIEF COMPLIANCE OFFICER COMMITTEE No. 50-05 COMPLIANCE MEMBERS No. 6-05 SEC RULES MEMBERS No. 81-05 SMALL FUNDS MEMBERS No. 60-05 TECHNOLOGY ADVISORY COMMITTEE No. 14-05 TRANSFER AGENT ADVISORY COMMITTEE No. 32-05 RE: NEW YORK BAR SUBMITS RULEMAKING PETITION TO SEC REGARDING RETENTION AND PRODUCTION OF E-MAIL BY INVESTMENT ADVISERS The Committee on Investment Management Regulation of the Association of the Bar of The City of New York has submitted a rulemaking petition to the Securities and Exchange Commission relating to the retention and production of e-mail by investment advisers.\* As summarized below, the Committee's petition requests that the Commission provide formal guidance through the rulemaking process on several issues relating to the books and records requirements of Rule 204-2 under the Investment Advisers Act of 1940, including: (i) investment adviser compliance with the records retention requirements as they apply to email; and (ii) email production in response to SEC inspection requests. APPLICATION OF RETENTION REQUIREMENTS TO E-MAIL The Committee's petition seeks formal Commission guidance regarding adviser compliance with the retention requirements of Rule 204-2 as they apply to e-mail. The petition notes that although the SEC staff has indicated that advisers that do not retain all e-mail must put into place procedures reasonably designed to ensure that required information is retained, many advisers still feel compelled to keep all e-mail communications for five years for fear that SEC inspectors will either deem the adviser's procedures unreasonable or will insist on absolute certainty that all required records have not been deleted. The petition expresses concern that maintaining all of a firm's e-mail for five years is becoming increasingly burdensome given the explosive growth in the use of e-mails. The petition notes that this situation could be eased by a \* See Letter from the Association of the Bar of the City of New York to Jonathan G. Katz, Secretary, SEC, dated May 11, 2005 (copy attached). The Committee's petition acknowledges that the SEC staff may be preparing some form of written guidance on this subject, but notes that the issues of e-mail retention and production should be addressed through the public rulemaking process instead. 2 more formal statement from the Commission stating that reasonable procedures will satisfy an adviser's retention requirement with respect to e-mail and giving guidance as to the types of procedures the

Commission would view as reasonable. The petition also requests that the Commission clarify that such procedures should not include a requirement for an adviser to review every e-mail individually prior to deletion, given the financial burden resulting from such review. The Committee's petition notes that adding to the confusion over what email must be retained is Rule 204-2(a)(7), which requires retention of certain types of written communications. The petition explains that while many in the advisory industry have long interpreted this rule as only applying to communications between an investment advisory firm and third parties, some of the staff of the SEC's Office of Compliance Inspections and Examinations have taken the position that the rule also applies to communications among a firm's employees. The petition notes that given the large volume of e-mail traffic sent among employees every day, complying with the staff position would impose a significant burden on the resources of many advisory firms. The petition also refers to the literal text in the rule, which speaks only of communications "received and ... sent by" an adviser, not of communications within a firm. Accordingly, the petition urges the Commission to affirm the long-standing industry interpretation that Rule 204-2(a)(7) applies only to communications with third parties.

**E-MAIL PRODUCTION IN RESPONSE TO INSPECTION REQUESTS**

The Committee's petition seeks formal Commission guidance relating to e-mail production in response to inspection requests. The petition points out that SEC inspectors routinely request that an adviser promptly produce all firm e-mail, or all email sent or received by certain individuals, in an electronically searchable format. These requests raise two issues: (i) whether the Commission has the authority to inspect all adviser records; and (ii) whether the Commission can require all records to be produced in a specific format. Regarding Commission authority, the petition notes that the SEC has taken the position that Section 204 of the Advisers Act allows it to review any record of an adviser, whether or not required to be retained by Rule 204-2. The petition submits that Section 204 authorizes the Commission to require by rule that advisers retain records that it deems necessary to protect investors and to inspect the records it requires investment advisers to retain. As such, the petition requests that the Commission consider addressing the issue through formal rulemaking and not try to create law through the inspection and enforcement process. Regarding required formatting, the petition notes that only certain records are required to be kept in a particular electronic format. The petition adds that although Rule 204-2(g) provides that required records maintained electronically must be arranged in a way that permits easy access and location, that requirement does not apply to records that are not required to be retained. Thus, the petition submits that advisory firms may, until required to do otherwise by rule or regulation, produce non-required electronic records to the SEC staff in any format or medium.

Barry E. Simmons Associate Counsel Attachment (in .pdf format)

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