

MEMO# 8597

January 29, 1997

SEC PROPOSES NEW DEFINITIONS OF ""SMALL BUSINESS"" IN CONNECTION WITH RULEMAKING UNDER THE FEDERAL SECURITIES LAWS

January 29, 1997 TO: CLOSED-END INVESTMENT COMPANY COMMITTEE No. 2-97
INVESTMENT ADVISERS COMMITTEE No. 5-97 SEC RULES COMMITTEE No. 11-97 SMALL
FUNDS COMMITTEE No. 2-97 UNIT INVESTMENT TRUST COMMITTEE No. 4-97 RE: SEC
PROPOSES NEW DEFINITIONS OF ""SMALL BUSINESS"" IN CONNECTION WITH RULEMAKING
UNDER THE FEDERAL SECURITIES LAWS

The Securities and Exchange Commission has proposed for public comment amendments to the definitions of "small business" and "small organization" that are used in connection with Commission rulemaking under the federal securities laws, including the Investment Company Act and the Investment Advisers Act. These definitions are used specifically for purposes of the Regulatory Flexibility Act, which requires the Commission to consider the impact of its regulations on small entities. The Commission is proposing amendments to these definitions to reflect recent changes in the law as well as changes in the securities markets over the past decade. The proposed amendments with respect to the Investment Company Act and the Advisers Act are summarized below and a copy of the Commission's release is attached. Comments on the proposed amendments must be filed with the Commission within thirty days from the date of publication in the Federal Register. Investment Company Act Rule 0-10 under the Investment Company Act currently defines "small business" or "small organization" to include each investment company that has \$50 million or less in assets as of the end of its most recent fiscal year. Recognizing that a definition that focuses only on the investment company's own assets may no longer be appropriate given that most investment companies today are part of a "family of funds," the Commission has proposed to amend Rule 0-10 to treat an investment company as a small entity only if it and other investment companies in its related group (as proposed to be defined in the rule) have net assets of \$50 million or less in the aggregate. With respect to this proposal, the Commission requests comment on the proposed definition of a group of related funds, on the appropriateness of the \$50 million threshold and on whether the test should be based on something other than asset size. (See pp. 18-19 of the attached release.) Investment Advisers Act Rule 0-7 under the Investment Advisers Act currently defines "small business" or "small organization" to include each investment adviser that either (i) manages client assets with a total value of \$50 million or less as of the end of its most recent fiscal year, and performs no other advisory services; or (ii) performs other advisory services, manages clients assets of \$50 million or less if it manages client funds,

and has assets related to its advisory business that do not exceed \$50,000. Because Congress did not intend affiliates of large businesses to receive benefits under the Regulatory Flexibility Act, the Commission is proposing to amend Rule 0-7 to deem an adviser to be "affiliated" with a large firm when the adviser controls, is controlled by, or is under common control with such firm. In addition, the amendments would simplify Rule 0-7 by applying the \$50,000 business asset test to all advisers, rather than solely to advisers that render services other than or in addition to managing client assets. In connection with the proposed amendments to Rule 0-7, the Commission requests comment on whether the proposed treatment of advisers affiliated with large firms properly focuses only on control affiliations, on the appropriateness of the thresholds of \$50 million for client assets and \$50,000 for business assets and, in particular, on whether the \$50 million threshold should be reduced to \$25 million in light of the recently-enacted legislation transferring to states primary responsibility for regulating "small" advisers (i.e., advisers with less than \$25 million under management). (See pp. 22-23 of the attached release.) Amy B.R. Lancellotta Associate Counsel Attachment (in .pdf format)

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