

MEMO# 10096

July 6, 1998

SEC PROPOSAL REGARDING INVESTMENT ADVISER YEAR 2000 REPORTS

1 Investment Adviser Year 2000 Reports, SEC Release No. IA-1728, IC-23293; File No. S7-20-98 (June 30, 1998) (the "Release"). The Release is a follow-up to two earlier companion releases in which the SEC proposed Year 2000 reporting requirements for certain transfer agents and broker-dealers. See Memorandum to Accounting/Treasurers Committee No. 13-98, Compliance Advisory Committee No. 8-98, Independent Accountants Advisory Committee No. 3-98, Internal Audit Committee No. 2-98, Investment Advisers Committee No. 10-98, Operations Committee No. 13-98, SEC Rules Committee No. 23-98, Transfer Agent Advisory Committee No. 14-98, Unit Investment Trust Committee No. 9-98, and Electronic Commerce Working Group, dated March 10, 1998. [10096] July 6, 1998 TO: ACCOUNTING/TREASURERS COMMITTEE No. 27-98 COMPLIANCE ADVISORY COMMITTEE No. 18-98 INDEPENDENT ACCOUNTANTS ADVISORY COMMITTEE No. 7-98 INTERNAL AUDIT COMMITTEE No. 6-98 INVESTMENT ADVISERS COMMITTEE No. 24-98 OPERATIONS COMMITTEE No. 26-98 SEC RULES COMMITTEE No. 68-98 TRANSFER AGENT ADVISORY COMMITTEE No. 37-98 UNIT INVESTMENT TRUST COMMITTEE No. 21-98 ELECTRONIC COMMERCE WORKING GROUP TECHNOLOGY TASK FORCE RE: SEC PROPOSAL REGARDING INVESTMENT ADVISER YEAR 2000 REPORTS

The Securities and Exchange Commission recently issued a release proposing a new rule and form under the Investment Advisers Act of 1940 that would require most registered investment advisers to file with the Commission status reports on their Year 2000 readiness. 1 Proposed new Rule 204-5 under the Advisers Act would require the filing of two reports, each on proposed new Form ADV-Y2K. The initial report would be filed no later than thirty days after the rule becomes effective; the second report would be filed no later than eight months from the date of the first filing. The proposed new rule and form are attached, and are summarized below. Comments on this proposal are due to the SEC by Monday, August 10, 1998. If there are issues you would like the Institute to consider addressing in its comment letter, please contact me by phone at (202) 326-5923, by fax at (202) 326-5839, or by e-mail at simmonbe@ici.org by Friday, July 17th. 2 The Release notes that this approach would permit multiple advisers to funds in a single fund complex to decide among themselves which adviser will be responsible for completing Part II with respect to that complex. 3 This is in recognition of the fact that under Section 204 of the Advisers Act, the Commission has the statutory authority to require only advisers to file such reports. 4 Part II would require information in these areas with respect to funds. 5 The six steps include: (i) awareness of potential Year 2000 problems; (ii) assessment of steps advisers and funds must take to avoid Year 2000 problems; (iii) implementation of the steps to avoid Year 2000 problems; (iv) internal testing of software designed to avoid Year 2000 problems; (v) point-to-point testing of software designed to avoid Year 2000 problems (i.e., testing with

service providers such as broker-dealers, custodians, transfer agents and distributors); and (vi) implementation of tested software that will avoid Year 2000 problems. Proposed Requirements As proposed, the filing requirement would apply to each registered investment adviser that: (a) has at least \$25 million of assets under management (as reported on Schedule I of the adviser's most recently filed Form ADV, or the most recent amendment to Form ADV); or (b) is an adviser to a registered investment company. Proposed Form ADV-Y2K consists of two parts. Part I would be completed by all respondents and would contain eleven questions about the adviser's Year 2000 preparations with respect to each of its clients. The questions all would be in multiple choice or fill-in-the-blank format. Part II is similar to Part I and would be completed by advisers to a registered fund or a group of registered funds. The Instructions to Part II specify that each adviser (or sub-adviser) to a fund must complete Part II with respect to an entire complex if the adviser advises a single fund (or a series) in the complex. The adviser, however, need not complete Part II for the complex or a fund (or a series) with respect to which another adviser is completing Part II.² An adviser responding to Part II on behalf of multiple complexes would complete multiple versions of Part II, one for each complex. The Release adds that in some cases, a third-party administrator that is not a registered investment adviser may be in the best position to report on Year 2000 readiness of the complex. If so, the administrator may complete the form on behalf of one of the advisers to a fund in the complex, but the adviser would be obligated to file the report.³ The Instructions to the form would require that the report be signed by an authorized person that participates in managing or directing the adviser's affairs. In terms of content, proposed Form ADV-Y2K would require each responding investment adviser to provide information relating to the following six areas:⁴ (1) the scope and status of the adviser's Year 2000 compliance plan; (2) the commitment by the adviser of resources and personnel (including consultants) to address Year 2000 issues; (3) the systems that may be affected by the Year 2000 problem; (4) progress on each of the six steps of preparation identified in the Release⁵; (5) contingency plans in the event that the adviser experiences Year 2000 difficulties after December 31, 1999; and (6) the readiness of third parties upon whom the adviser relies for critical systems. In stark contrast to the broker-dealer and transfer agent proposals, proposed Form ADV-Y2K would not require an attestation by an independent public accountant. In recognition that an adviser or a fund may rely on multiple systems that are at different stages of Year 2000 preparation, the Release requests the reporting adviser to base its responses on a qualitative average of its systems -- giving greater weight to mission-critical systems -- in order to present the most accurate picture practicable of the preparedness of the systems of the adviser or the fund. In requiring a qualitative average, the Release notes that the Commission "intends to be flexible and take a common sense approach." The Release notes that advisers would be required to file Form ADV-Y2K by facsimile, using numbers provided by the instructions to the form. No paper filings of the form would be accepted. Finally, consistent with the approach taken in the broker-dealer and transfer agent proposals, the Release states that the Commission intends to make the reports publicly available, "like all forms filed with the Commission by investment advisers."⁶ Requests for Comment Among other things, the Commission requests comment on the following issues: 1. Whether it is appropriate to permit multiple advisers to funds in a single complex to decide among themselves which adviser will be responsible for completing Part II of Form ADV-Y2K with respect to the complex; 2. Whether an attestation by an independent public accountant should be required; 3. Whether alternative ways to request information for multiple systems is desirable (e.g., on a system-by-system basis rather than a qualitative average); and 4. Whether the Commission's assumption that all advisers required to file the Form ADV-Y2K will be able to do so easily by facsimile is valid.

Barry E. Simmons Assistant Counsel Attachment

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