

MEMO# 5502

January 19, 1994

SEC PROPOSES AMENDMENTS TO FORM ADV TO REQUIRE DISCLOSURE REGARDING WRAP FEE AND ASSET ALLOCATION PROGRAMS

1January 19, 1994 TO: INVESTMENT ADVISERS COMMITTEE NO. 4-94 SEC RULES COMMITTEE NO. 9-94 RE: SEC PROPOSES AMENDMENTS TO FORM ADV TO REQUIRE DISCLOSURE REGARDING WRAP FEE AND ASSET ALLOCATION PROGRAMS

The Securities and Exchange Commission ("SEC") has issued for comment proposed revisions to Form ADV and rules under the Investment Advisers Act of 1940 to define the disclosures that should be made to investors by sponsors of wrap fee programs. This proposal was prepared in cooperation with the North American Securities Administrators Association ("NASAA"), which recently issued for comment a similar proposal. (See Memorandum to Investment Advisers Committee No. 33-93 and SEC Rules Committee No. 100-93, dated November 5, 1993.) A copy of the SEC release is attached. Scope of the Proposal As proposed by the SEC, Form ADV would be amended to add a new Schedule H. Schedule H would be required to be completed by a sponsor of a program under which any client is charged a specified fee or fees not based directly upon the transactions in the client's account for investment advisory services and execution of transactions. In addition, a sponsor of a mutual fund asset allocation program for which the sponsor or a related person (as defined in Form ADV) serves as an investment adviser, principal underwriter, or administrator would be required to complete the Schedule. Proposed Disclosure The following disclosure would be required by Schedule H: the sponsor's name, address, phone number along with a legend set forth in paragraph (a) of Item 8; detailed information on fees and costs; an explanation of how the program's managers are selected and reviewed and the circumstances under which they will be replaced; information about verification of performance, or, if performance is not verified, a statement to that effect; a description of the client information provided to the portfolio manager; and, any restrictions on the ability of clients to contact and consult with portfolio managers. Advisers that sponsor or participate in mutual fund wrap fee programs are not required to include information on portfolio managers in their brochures. Instead, they must explain how the adviser develops recommendations regarding the allocation of client assets among mutual funds. In addition to this information, the sponsor must, in narrative form in the brochure, include certain specified information from Part II of the Form ADV. This information includes the items from Part II relating to: other business activities and time spent thereon; other financial industry activities or affiliations; education and business standards and background; participation or interest in client transactions as a principal or as a broker or agent for a third party; conditions for managing an account;

review of accounts; and additional compensation. 2Proposed Amendment to Rule 204-3 The SEC has proposed to amend Rule 204-3 under the Advisers Act, the "brochure rule", to require an investment adviser, in lieu of the disclosure currently required by the Rule, to furnish each client and prospective client of a wrap fee program "with a written disclosure statement containing at least the information required by Schedule H of Form ADV." * * * *
* * * As mentioned above, the SEC's proposal is substantially similar to a proposal recently issued by NASAA. In its comment letter on the NASAA proposal, the Institute expressed concern that the proposal included in its scope mutual fund asset allocation programs in which the sponsor is affiliated with an investment company. The Institute's letter discussed the differences between wrap fee and mutual fund asset allocation programs and explained that under current law, clients of a mutual fund asset allocation program are provided sufficient information concerning the program, its sponsor, its affiliation with an investment company, and the fees charged by the adviser. Based on the foregoing, the Institute recommended that the scope of the proposal be amended to exclude mutual fund asset allocation programs and thus be limited solely to wrap fee programs. A copy of the Institute's comment letter on the NASAA proposal is attached. Comments on the SEC's proposal are due no later than March 7, 1994. If you have any comments on the proposed amendments which 3you would like to have included in the Institute's comment letter, please provide them to me by Tuesday February 15, 1994. My direct dial number is 202/326-5825. Tamara K. Cain Assistant Counsel Attachments