

MEMO# 10354

October 6, 1998

SEC ADOPTS YEAR 2000 RULE FOR INVESTMENT ADVISERS

1 Investment Adviser Year 2000 Reports, SEC Release Nos. IA-1769 and IC-23476; File No. S7-20-98 (Oct. 1, 1998) (the "Release"). 2 See Investment Adviser Year 2000 Reports, SEC Release Nos. IA-1728 and IC-23293; File No. S7-20-98 (June 30, 1998). 3 The Release also notes that the Commission has provided a list of frequently asked questions and answers about new Form ADV-Y2K on its Internet web site to assist advisers in completing the form. The list is attached and can also be accessed at the following location: <http://www.sec.gov/rules/other/advfaq.htm>. 4 Despite concerns raised by commenters about duplicative reporting, the Release notes that the rule does not exempt from the filing requirement those advisers that are also registered broker-dealers or transfer agents, or affiliates of banks. [10354] October 6, 1998 TO: ACCOUNTING/TREASURERS MEMBERS No. 28-98 COMPLIANCE ADVISORY COMMITTEE No. 32-98 INDEPENDENT ACCOUNTANTS ADVISORY COMMITTEE No. 10-98 INTERNAL AUDIT COMMITTEE No. 11-98 INVESTMENT ADVISER MEMBERS No. 30-98 OPERATIONS MEMBERS No. 27-98 SEC RULES MEMBERS No. 80-98 TRANSFER AGENT ADVISORY COMMITTEE No. 63-98 UNIT INVESTMENT TRUST MEMBERS No. 25-98 ELECTRONIC COMMERCE WORKING GROUP TECHNOLOGY TASK FORCE RE: SEC ADOPTS YEAR 2000 RULE FOR INVESTMENT ADVISERS

The Securities and Exchange Commission recently adopted a new rule and form under the Investment Advisers Act of 1940 ("Advisers Act") that requires most registered advisers to file with the Commission Year 2000 readiness reports.¹ The rule is adopted largely as was earlier proposed.² A copy of the new rule and form are attached, and they are summarized below.³ Rule 204-5 New rule 204-5 under the Advisers Act requires each registered adviser that (i) has at least \$25 million of assets under management, or (ii) is an adviser to a registered investment company to file new Form ADV-Y2K with the Commission.⁴ The form must be filed no later than December 7, 1998, and an updated form must be filed no later than June 7, 1999. The information in each filing must be current as of a date no earlier than two weeks before the respective filing deadline. In addition, the form must be signed by an authorized person of the adviser that participates in managing or directing the adviser's affairs. It does not have to be accompanied by an attestation report prepared by an independent public accountant. The forms will be made available to ⁵ The Release notes that item (7) was added due to the important role advisers can play in identifying issuers and securities that may be adversely affected by Y2K problems, and protecting their clients from losses as a result. The Commission recognized, however, that some advisers have investment styles that make consideration of Y2K preparedness of issuers irrelevant, such as (i) those advisers whose advice is limited to the advisability of investing in broad asset classes, such as market timers, (ii) those advisers who manage accounts that track indexes,

and (iii) those advisers who use “technical analysis” and base their advice on market trends, but not on the fundamentals of particular issuers. The Release notes that these advisers would respond to this item by checking the “Not Applicable” response, provided that such response is appropriate with respect to all of the adviser’s accounts. 6 See Release at n. 27. 7 Release at n. 13. the public. Form ADV-Y2K As was proposed, Form ADV-Y2K contains two parts. The first part must be completed by all advisers required to file the form, whereas the second part must be completed only by advisers to registered investment companies. Part I contains thirteen questions -- all in multiple choice or fill-in-the-blank format, and elicits information in the following areas: (1) the adviser’s Y2K compliance plan; (2) resources and personnel to address Y2K issues; (3) systems that may be affected; (4) the adviser’s progress in addressing Y2K issues; (5) contingency plans; (6) the readiness of third parties; and (7) whether, and the means by which, the adviser takes into consideration the Y2K preparedness of issuers of securities the adviser recommends to clients.⁵ As was recommended by the Institute in our comment letter on the proposed rule, the form requires only advisers that are sponsors or administrators of a fund complex to complete Part II. If no sponsor or administrator of the complex is a registered adviser, however, the rule requires that at least one adviser to a fund (or series) in the complex must submit a report for the fund complex, if the adviser is registered with the Commission. In addition, despite commenters’ concerns that an adviser should not be required to report on the Y2K readiness of third parties, the Commission decided to leave unchanged the questions in the form that elicit this information and has added an instruction to the form that requires advisers to make reasonable inquiries of third parties to obtain their Y2K status. The Release adds that “reasonable inquiries” can be satisfied by “analyzing the response to questionnaires sent to third parties.”⁶ In recognition of concerns that proposed Part II did not accurately reflect the investment company organizational structure, the Commission has modified Part II to clarify any ambiguities. As was proposed, the form provides that where there are multiple computer systems for which different amounts of progress have been made in becoming Y2K compliant, the responses should be based on a qualitative average of the systems. Finally, the instructions to the form permit the form to be completed either manually, by completing a paper version of the form, or electronically, by completing the version of the form on the Commission’s web site. The instructions also require that advisers file an original and two copies of each form. Although the Commission had considered requiring advisers to file the form by fax, the Release indicates that the Commission is not doing so because “we are unsure about the ability of the technology we had planned to use to accept the expected volume of filings.”⁷ Barry E. Simmons Assistant Counsel Attachment Note: Not all recipients of this memo will receive an attachment. If you wish to obtain a copy of the attachment referred to in this memo, please call the Institute's Library Services Division at (202)326- 8304, and ask for this memo's attachment number: 10354.

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