

***Transmittal******TR-360***

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**Number TR-360**

On May 7, 2004, the SEC published proposed regulations in the Federal Register that provide a narrow exemption from Investment Adviser registration to thrifts that agree to limit their investment management and advisory services to a limited range of accounts. Under the proposal, a thrift's fiduciary accounts are segregated into two categories. Thrifts that provide services to accounts that include only traditional trust, estate, and guardianship accounts will be exempt from registration. Thrifts providing services to accounts that include investment management agency accounts, revocable trusts and other accounts that the SEC has defined as not being for a fiduciary purpose will be required to register as an investment adviser. Thrifts with trust powers should consider filing comments with the SEC on the proposal. The comment period closes on July 9, 2004.

## SECURITIES AND EXCHANGE COMMISSION

### 17 CFR Parts 240, 275 and 279

[Release Nos. 34-49639, IA-2232; File No. S7-20-04]

RIN 3235-A116

### Certain Thrift Institutions Deemed Not To Be Investment Advisers

**AGENCY:** Securities and Exchange Commission.

**ACTION:** Proposed rule.

**SUMMARY:** The Securities and Exchange Commission ("Commission") is publishing for comment a new rule under the Investment Advisers Act of 1940 that would address the application of the Act to certain thrift institutions, and a new rule under the Securities Exchange Act of 1934 addressing thrift institutions' collective trust funds.

**DATES:** Comments should be received on or before July 9, 2004.

**ADDRESSES:** Comments may be submitted by any of the following methods:

#### Electronic Comments

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/proposed.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number S7-20-04 on the subject line; or
- Use the Federal eRulemaking Portal (<http://www.regulations.gov>). Follow the instructions for submitting comments.

#### Paper Comments

- Send paper comments in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-0609. All submissions should refer to File Number S7-20-04. This file number should be included on the subject line if e-mail is used. To help us process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/proposed.shtml>). Comments are also available for public inspection and copying in the Commission's Public Reference Room, 450 Fifth Street, NW., Washington, DC 20549. All comments received will be posted without change; we do not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly.

**FOR FURTHER INFORMATION CONTACT:** Robert Tuleya, Attorney-Adviser, Jamey

Basham, Branch Chief, or Jennifer Sawin, Assistant Director, at (202) 942-0719 or [IRules@sec.gov](mailto:IRules@sec.gov), Office of Investment Adviser Regulation, Division of Investment Management, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-0506.

**SUPPLEMENTARY INFORMATION:** The Commission is requesting public comment on proposed rule 202(a)(11)-2 under the Investment Advisers Act of 1940 (15 U.S.C. 80b), and on proposed rule 12g-6 under the Securities Exchange Act of 1934 (15 U.S.C. 78a *et seq.*).

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#### Executive Summary

The Commission is proposing a new rule under the Investment Advisers Act of 1940 ("Advisers Act" or "Act") that would exempt thrifts from the Act when they provide investment advice as part of certain trust department fiduciary services. Under the rule, a thrift institution would be deemed not to be an investment adviser if its investment advisory services are provided solely in its capacity as trustee, executor, administrator, or guardian for customer accounts created and maintained for a fiduciary purpose, or to its collective trust funds excepted from the Investment Company Act of 1940 ("Investment Company Act"). The Commission is also proposing to exempt thrift institutions' collective trust funds from the registration and reporting requirements of the Securities Exchange Act of 1934 ("Exchange Act").

#### I. Discussion

The Advisers Act regulates the activities of certain "investment advisers," defined generally by section 202(a)(11) of the Act as persons whose regular business involves providing others with advice about securities for

compensation.<sup>1</sup> Under the Act, investment advisers are fiduciaries who must fully disclose any material conflict that they have with their clients.<sup>2</sup> Advisers must register with the Commission,<sup>3</sup> provide their clients with an informational brochure,<sup>4</sup> maintain records related to their advisory activities,<sup>5</sup> and submit to periodic examination by our staff.<sup>6</sup>

Banks (and bank holding companies) are excepted from the definition of investment adviser by section 202(a)(11)(A) of the Act.<sup>7</sup> The Act, however, contains no exception for thrift institutions,<sup>8</sup> which are not "banks" as defined by the Act.<sup>9</sup> As a

<sup>1</sup> 15 U.S.C. 80b-2(a)(11). See Applicability of the Investment Advisers Act to Financial Planners, Pension Consultants, and Other Persons Who Provide Investment Advisory Services as a Component of Other Financial Services, Investment Advisers Act Release No. 1092 (Oct. 8, 1987) (52 FR 38400 (Oct. 16, 1987)) ("Release IA-1092").

<sup>2</sup> See *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 194 (1963) (an investment adviser is a fiduciary who owes his clients "an affirmative duty of 'utmost good faith, and full and fair' disclosure of all material facts") ("*Capital Gains*").

<sup>3</sup> 15 U.S.C. 80b-3. Generally, following the enactment of the National Securities Markets Improvement Act of 1996 ("NSMIA") (Pub. L. No. 104-290, 110 Stat. 3428) (1996), only larger advisers that have \$25 million or more of assets under management, or that advise investment companies, register with the Commission. Smaller advisers register with state securities authorities under state law. See section 203A of the Advisers Act (15 U.S.C. 80b-3a); Rules Implementing Amendments to the Investment Advisers Act of 1940, Investment Advisers Act Release No. 1633 (May 15, 1997) (62 FR 28112 (May 22, 1997)).

<sup>4</sup> 17 CFR 275.204-3.

<sup>5</sup> 15 U.S.C. 80b-4 and 17 CFR 275.204-2.

<sup>6</sup> 15 U.S.C. 80b-4.

<sup>7</sup> 15 U.S.C. 80b-2(a)(11)(A). Provisions of the Gramm-Leach-Bliley Act narrowed this bank exception, so that a bank is an "investment adviser" under the Advisers Act to the extent that it advises registered investment companies. Either the bank itself or a separately identifiable department or division of the bank must register as an investment adviser. The registered adviser is subject to all requirements of the Advisers Act. Pub. L. No. 106-102, 113 Stat. 1338, §217 (1999) (codified in relevant part at 15 U.S.C. 80b-2(a)).

<sup>8</sup> In this release, the term "thrift institution" or "thrift" includes federal savings associations, federal savings banks, and state savings associations. See *infra* note 40.

<sup>9</sup> A "bank" under section 202(a)(2) of the Advisers Act (15 U.S.C. 80b-202(a)(2)) includes national banks, members of the Federal Reserve System, and other banks and trust companies having similar authority to national banks and supervised by state or federal banking agencies. We have consistently interpreted "bank" as not including savings associations, see Status of Savings and Loan Associations Under the Federal Securities Laws, Investment Company Act Release No. 13666 (Dec. 12, 1983) (48 FR 56061 (Dec. 19, 1983)) ("Release IC-13666"), and federal thrift regulators have acknowledged this interpretation. Fiduciary Powers of Federal Savings Associations; Community Reinvestment Act, Office of Thrift Supervision Release No. 97-68 (July 14, 1997) (62 FR 39477 (July 23, 1997)) ("Although banks are exempt from the Investment Advisers Act, Federal savings associations are not.") ("OTS Fiduciary Powers Proposing Release").

result, a thrift that manages securities portfolios or provides other types of investment advisory services for its customers in connection with its trust operations is generally subject to the Act.

The absence of a thrift exception in the Advisers Act can, we believe, be explained by historical context. When Congress enacted the Advisers Act in 1940, federal savings associations, for example, were not authorized to provide the types of services that would subject them to the Act.<sup>10</sup> It was not until 1980 that Congress gave federal savings associations the authority to provide trust services, including the authority to act as an investment adviser.<sup>11</sup> Today, thrifts may be granted trust powers similar to those of national banks.<sup>12</sup> Such thrift trust activities also are subject to similar regulation and supervision by the Office of Thrift

Supervision ("OTS").<sup>13</sup> When they serve as trustees, thrifts and banks are both also subject to state trust laws.<sup>14</sup>

Recently, both Congress and the Commission have recognized that thrift trust powers and activities have converged with those of banks. In 1999, in the Gramm-Leach-Bliley Act, Congress amended the definition of "bank" in the Investment Company Act to include thrifts.<sup>15</sup> As a result, common

and collective trust funds sponsored by thrifts are now excepted from the definition of "investment company" under the Investment Company Act, subject to the same limitations and conditions as bank common and collective trust funds.<sup>16</sup> In May of 2001, we adopted a new rule exempting thrifts from the definitions of "broker" and "dealer" under the Exchange Act, under the same terms and conditions that apply to banks.<sup>17</sup>

Thrift industry participants,<sup>18</sup> a member of Congress,<sup>19</sup> and the OTS<sup>20</sup>

Insurance Act, and are therefore "banks" for purposes of the Investment Company Act. 12 U.S.C. 1813(c).

<sup>16</sup>The Gramm-Leach-Bliley Act also clarified that the scope of the Investment Company Act's bank common trust fund exception is limited to common trust funds operated solely as an aid to a bank's administration of trust or other accounts maintained for a "bona fide" fiduciary purpose. See Pub. L. 106-102, 113 Stat. 1338, section 221 (1999) (codified in relevant part at 15 U.S.C. 80a-3(c)(3)). Previously, our staff interpreted the scope of the common trust fund exception in the same manner. See *infra* notes 46 and 53-56 (discussing the long-standing staff interpretation of the bank common trust fund exception).

<sup>17</sup>Definition of Terms in and Specific Exemptions for Banks, Savings Associations, and Savings Banks Under Sections 3(a)(4) and 3(a)(5) of the Securities Exchange Act of 1934, Securities Exchange Act Release No. 44291 (May 11, 2001) (66 FR 27760 (May 18, 2001)) ("Exchange Act Release No. 44291"). Rule 15a-9 gave thrifts the same exemptions as banks from the "broker" and "dealer" definitions. 17 CFR 240.15a-9. Rule 15a-7 under the Exchange Act gave banks a temporary exemption from complying with changes made by the Gramm-Leach-Bliley Act to the Exchange Act's definitions of "broker" and "dealer." 17 CFR 240.15a-7. We have adopted final rules defining "dealer," Definition of Terms in and Specific Exemptions for Banks, Savings Associations, and Savings Banks under Sections 3(a)(4) and 3(a)(5) of the Securities Exchange Act of 1934, Exchange Act Release No. 47364 (Feb. 13, 2003), and have extended the temporary exemption from the definition of "broker" until November 11, 2004. Order Extending Temporary Exemption of Banks, Savings Associations, and Savings Banks from the Definition of "Broker" Under Section 3(a)(4) of the Securities Exchange Act of 1934; Notice of Intent to Amend Rules, Securities Exchange Act Release No. 47649 (April 8, 2003).

<sup>18</sup>Letter from Patricia R. Hatler, Senior Vice President and General Counsel, Office of General Counsel, Nationwide Insurance-Nationwide Financial, to Jonathan G. Katz, Secretary, U.S. Securities and Exchange Commission (July 12, 2001); Letter from Diane M. Casey, President and Chief Executive Officer, America's Community Bankers, to Paul F. Roye, Director, Division of Investment Management, U.S. Securities and Exchange Commission (July 31, 2001). These letters are available for inspection and copying in the Commission's Public Reference Room, 450 5th Street, NW., Washington, DC (File No. S7-20-04).

<sup>19</sup>Letter from The Honorable Evan Bayh, United States Senator (Indiana), to Arthur Levitt, Chairman, U.S. Securities and Exchange Commission (Aug. 18, 2000). This letter is available in File No. S7-20-04.

<sup>20</sup>Letter from Scott L. Albinson, Managing Director, Office of Supervision, Office of Thrift Supervision, to Annette L. Nazareth, Director, Division of Market Regulation and Paul F. Roye,

<sup>10</sup>We use the term "federal savings association" to mean any federal savings association or federal savings bank chartered under section 5 of the Home Owners' Loan Act [12 U.S.C. 1464]. See 12 U.S.C. 1813(b)(2). See also 12 U.S.C. 1462(5).

<sup>11</sup>The Depository Institutions Deregulation and Monetary Control Act of 1980 ("Monetary Control Act") first authorized a grant of trust powers to federal savings associations. Pub. L. No. 96-221, 94 Stat. 132 (1980) (codified in relevant part at 12 U.S.C. 1464(n)). Specifically, the Monetary Control Act authorized the Federal Home Loan Bank Board ("FHLBB"), the predecessor to the Office of Thrift Supervision ("OTS"), to grant federal savings association charters that included fiduciary powers. Pursuant to this authority, the FHLBB issued regulations in December 1980 governing federal savings associations' fiduciary activities. *Trust Powers*, Federal Home Loan Bank Board Resolution No. 80-738 (Nov. 26, 1980) [45 FR 82162 (Dec. 15, 1980)]. These rules, which currently appear in Title 12, part 550 of the Code of Federal Regulations ("Part 550"), have been interpreted to apply to federal savings associations' investment advisory services. OTS Fiduciary Powers Proposing Release, *supra* note 9.

<sup>12</sup>Compare 12 U.S.C. 92a(a) (authorizing the Office of the Comptroller of the Currency ("OCC") to grant trust powers to national banks) with 12 U.S.C. 1464(n) (authorizing the OTS to grant trust powers to federal savings associations). See also S. Rep. No. 96-368, 96th Cong., 2d Sess. 13 (1979), reprinted in 1980 U.S.C.C.A.N. 236, 248 (stating that the Monetary Control Act permits [the OTS] the authority to grant federal savings associations the ability to offer trust services on the same basis as national banks).

Several states also have granted trust powers to state-chartered savings associations. See 205 Ill. Comp. Stat. Ann. 105/1-6 (permitting savings and loan associations to exercise all powers necessary to qualify as a trustee or custodian); Mich. Comp. Laws 491.506 (empowering savings associations to exercise trust powers upon application to and approval by the supervisor); N.J. Stat. Ann. 17:12B-48 (granting associations the power to apply to the commissioner for permission to act as trustee, executor, administrator, guardian); N.Y. Banking Law 380-H (McKinney) (authorizing banking board to allow savings and loan associations to have fiduciary capacity); Okla. Stat. tit. 18, § 381.54 (permitting savings and loan associations to have and exercise all such powers as conferred on federal savings associations).

<sup>13</sup>Federal savings associations providing trust services are subject to OTS regulations that require the proper exercise of savings association trust powers. See generally 12 CFR 550. In 1997, the OTS updated its fiduciary powers rules to conform them more closely to the rules issued by the Office of the Comptroller of the Currency at 12 CFR part 9.

Fiduciary Powers; Community Reinvestment Act, Office of Thrift Supervision Release No. 97-129 (Dec. 19, 1997) (62 FR 67696 (Dec. 30, 1997)) ["OTS Fiduciary Powers Final Rule"]. See also OTS Fiduciary Powers Proposing Release, *supra* note 9. The OCC itself comprehensively revised its rules governing the fiduciary powers of national banks in 1996. OTS Fiduciary Powers Proposing Release, *supra* note 9, citing 61 FR 68543 (Dec. 30, 1996). The OTS rules adopted in 1997 draw "extensively on the OCC's final rule and the comments the OCC received on its proposed rule." OTS Fiduciary Powers Proposing Release, *supra* note 9. Additional amendments made to the OTS' fiduciary powers rules in 2002 are also consistent with similar amendments adopted by the OCC. Recordkeeping and Confirmation Requirements for Securities Transactions; Fiduciary Powers of Savings Associations, Office of Thrift Supervision Release No. 2002-57 (Dec. 2, 2002) (67 FR 76293 (Dec. 12, 2002)) ["OTS Recordkeeping Rules Release"].

OTS regulations provide that state-chartered savings associations should follow the standards for exercise of trust powers contained in Part 550. 12 CFR 550.10(b)(1). These regulations also state that OTS examinations staff will monitor the fiduciary activities of state-chartered savings associations and may restrict or prohibit activities that threaten the safety and soundness of a state-chartered savings association. 12 CFR 550.10(b)(2).

<sup>14</sup>As trustees, thrifts and banks are subject to state trust law that governs their conduct and activities. See George Gleason Bogert & George Taylor Bogert, *The Law of Trusts and Trustees* § 541, at 159 (1993). Some states have codified trust law. E.g., Cal. Probate Code 16000-16082 (addressing duties of trustees); Ohio Rev. Code Ann. 2109.01-2109.68 (governing fiduciaries); 20 Pa. Cons. Stat. Ann. 7131-7136 (powers, duties and liabilities of trustees). See also Uniform Trust Code, Article 8 (2000) (amended 2002) (duties and powers of trustees). Federal laws and regulations governing bank and thrift trust powers refer expressly to state trust law. See 12 U.S.C. 92a(a) (authorizing the OCC to grant trust powers consistent with state trust laws); 12 U.S.C. 1464(n) (authorizing Director of the OTS to grant federal savings associations trust powers permitted under state law); 12 CFR 550.136 (clarifying the applicability of state law to federal savings associations); 12 CFR 550.10(b) ("state chartered savings association must conduct its fiduciary operations in accordance with applicable State law"). See also *supra* note 13.

<sup>15</sup>Pub. L. No. 106-102, 113 Stat. 1338, section 223 (1999) (codified in relevant part at 15 U.S.C. 80a-2(a)(5)). As amended by the Gramm-Leach-Bliley Act, section 2(a)(5) of the Investment Company Act defines a "bank" for purposes of the Investment Company Act to include any "depository institution" as that term is defined in the Federal Deposit Insurance Act. 15 U.S.C. 80a-2(a)(5). Savings associations are types of "depository institution" under the Federal Deposit

P=’25780’≤have called upon us to re-examine the status of thrifts under the Advisers Act. Some of these commenters have argued that, because thrift institutions have fiduciary powers similar to those of national banks and are similarly regulated, thrifts should be treated similarly to banks under the Advisers Act. These commenters have also argued that our new rule under the Exchange Act results in thrifts receiving different treatment under the Exchange Act than under the Advisers Act. Another commentator has suggested that it is inconsistent for a thrift to be subject to the Advisers Act when advising its common or collective trust funds that are excepted from the definition of “investment company” under the Investment Company Act.<sup>21</sup>

On the other hand, two groups of advisers have written us opposing expansion of the Advisers Act bank exception to include thrifts.<sup>22</sup> These groups assert that expanded relief would diminish investor protection by eliminating important safeguards that the Advisers Act provides to advisory clients, would be inconsistent with principles of functional regulation, and would create an unfair competitive advantage for thrifts that provide the same investment advisory services as other money managers and financial planners.<sup>23</sup>

In light of the convergence of bank and thrift trust powers and regulation, we are proposing a new rule that would

Director, Division of Investment Management, U.S. Securities and Exchange Commission (Mar. 30, 2001); Letter from Ellen Seidman, Director, Office of Thrift Supervision, to Harvey L. Pitt, Chairman, U.S. Securities and Exchange Commission (Dec. 3, 2001). These letters are available in File No. S7–20–04.

<sup>21</sup> See Barry P. Barbash, “The Gramm-Leach-Bliley Act of 1999 and the Investment Management Industry: A Brave New World of Regulation,” Materials for 2000 Mutual Funds and Investment Conference (Mar. 26–30, 2000), at XIII–9.

<sup>22</sup> Letter from David G. Tittsworth, Executive Director, Investment Counsel Association of America, to Harvey L. Pitt, Chairman, U.S. Securities and Exchange Commission (Dec. 27, 2001); Letter from Duane R. Thompson, Director of Government Relations, The Financial Planning Association, to Laura S. Unger, Acting Chairman, U.S. Securities and Exchange Commission (June 8, 2001). These letters are available in File No. S7–20–04.

<sup>23</sup> Letter from Duane R. Thompson, Director of Government Relations, The Financial Planning Association, to The Honorable Michael G. Oxley, Chairman, Committee on Financial Services, United States House of Representatives, The Honorable John J. LaFalce, Ranking Member, Committee on Financial Services, United States House of Representatives, The Honorable Spencer Bachus, Chairman, Subcommittee on Financial Institutions and Consumer Credit, United States House of Representatives, and The Honorable Maxine Waters, Ranking Member, Subcommittee on Financial Institutions and Consumer Credit, United States House of Representatives (Mar. 28, 2002). This letter is available in File No. S7–20–04.

provide a limited exception from the Advisers Act for thrifts. As described in more detail below, proposed new rule 202(a)(11)–2 would except thrift institutions from the Advisers Act to the extent they provide investment advice in their capacity as trustee, executor, administrator, or guardian. Under the proposed rule, the Act would continue to apply to a thrift institution to the extent the thrift provides other investment advisory services, including advising mutual funds, offering managed agency accounts,<sup>24</sup> or providing “retail” financial planning services. Thus, thrifts that offer advice only in the context of other fiduciary trust services would be excepted from the Advisers Act as are banks, while retail advisory services would continue to be subject to the federal securities laws much as retail brokerage services are.<sup>25</sup>

We are proposing this exception because we believe that the Advisers Act was not intended or designed to regulate certain advisory services provided only as part of these banking (and now thrift) trust services.<sup>26</sup> With respect to certain thrift trust relationships, the Advisers Act cannot be meaningfully applied because it does not work well *in those situations*.<sup>27</sup> The

<sup>24</sup> In a managed agency account, or investment management agency account, the thrift does not take legal title to the managed assets, as it would if it served as trustee. Instead, the thrift institution, like most investment advisers, gives investment advice to the owner of the assets, or manages those assets under power of attorney granted by the owner. An advisory account may be a managed agency account even though the managed assets are held in a trust; the trustee hires the investment adviser as agent, and is able to receive disclosure and provide client consent when needed.

<sup>25</sup> See *infra* note 31.

<sup>26</sup> We propose to adopt the rule pursuant to section 202(a)(11)(F) of the Act (15 U.S.C. 80b–2(a)(11)(F)), which gives us authority to except from the definition of “investment adviser” (and therefore from all the provisions of the Act) “such \* \* \* persons not within the intent of this paragraph, as the Commission may designate by rules and regulations or order.”

<sup>27</sup> We are proposing to except thrifts from the Advisers Act in circumstances where we believe Congress did not intend the Advisers Act to apply and the Act cannot meaningfully be applied. We note that these activities are subject to an alternative system of regulation under thrift regulation and trust law and subject to fiduciary duties imposed by those regulations and laws. See generally 12 CFR 550.10–550.620 (outlining standards applicable to the fiduciary activities of savings associations); *supra* notes 13 and 14. See also *OTS Trust and Asset Management Handbook*, at 110.1 (2001) (discussing responsibilities and duties owed by a fiduciary/trustee) (“OTS Trust Handbook”). We are not, however, suggesting that banking or thrift regulation generally provide protections equivalent to those afforded by the federal securities laws in other circumstances. The protections provided by the securities laws remain essential to adequately guard the interests of the investing public. See, e.g., *Concerning Financial Modernization Legislation: Hearings Before the*

Advisers Act permits advisory clients to protect themselves when their interests conflict with those of their investment adviser. The Advisers Act does this by requiring the adviser to obtain the client’s consent after giving the client full and fair disclosure of the conflict.<sup>28</sup> The Act implicitly presumes that the adviser has an identifiable client with identifiable interests, and that this client is competent to grant or withhold consent to conflicts that arise in the course of an advisory relationship. Thrift trust relationships, however, often involve settlors who have died, or beneficiaries who are minors or incompetents. Trust instruments may impose fiduciary obligations upon the thrift as trustee with respect to a number of beneficiaries who could be considered clients under the Advisers Act, some of whom may have competing interests, or even be unborn.<sup>29</sup> Trust law, and OTS regulations governing a savings association’s administration of fiduciary accounts over which the savings association exercises investment discretion, address these situations in which informed consent alone may not be effective to protect the interests of trust grantors and beneficiaries. These laws and regulations typically either require transactions presenting potential conflicts to be authorized by the trust instrument or impose procedural safeguards designed to prevent the conflicts from harming the trust.<sup>30</sup>

*Senate Comm. on Banking, Hous., and Urban Affairs*, 106th Cong., 1st Sess. (Feb. 24, 1999) (testimony of Arthur Levitt, Chairman, U.S. Securities and Exchange Commission). For example, the bank trust and fiduciary activities exception to the definition of “broker” in section 3(a)(4)(B)(II) of the Exchange Act makes clear that banks acting as brokers with respect to trust and fiduciary accounts by, among other things, being paid as brokers, must shift those accounts to a registered broker-dealer.

<sup>28</sup> Release IA–1092, *supra* note 1.

<sup>29</sup> For example, a life beneficiary’s consent to a trustee’s investment decision does not relieve the trustee of liability to the remainder beneficiaries for any defect in the decision. See, e.g., Austin Scott & William Fratcher, *The Law of Trusts* § 216.2 (1987).

<sup>30</sup> As discussed earlier, under the Advisers Act an adviser must disclose to clients all material facts regarding a potential conflict of interest “so that the client can make an informed decision as to whether to enter into or continue an advisory relationship with the adviser or whether to take some action to protect himself against the specific conflict of interest involved.” Release IA–1092, *supra* note 1. In comparison, the OTS has recognized that “[o]btaining the consent of all the [trust’s] beneficiaries may be difficult if more than one class of remaindermen exist or if the beneficiaries are minors, unborn, or otherwise unable to give informed consent. Under applicable state law, the savings association may need to have a guardian ad litem appointed for minors, the unborn, or the incompetent and obtain an order from the appropriate court approving the transaction.” OTS Thrift Bulletin 76–2 (May 15, 2001). Moreover, the OTS has stated, “[i]f a savings association pursues

We are not, however, proposing to give thrifts an unlimited exception from the Advisers Act. We adopted a broad exemption for thrifts under the Exchange Act in light of amendments to that Act that require most brokerage activities of banks to be provided through a registered broker-dealer.<sup>31</sup> The Advisers Act contains no similar or comparable "push out" provision. As a result, a general exception from the Advisers Act would except not only thrifts' trust department services to fiduciary purpose accounts and collective trust accounts, but would also except thrifts' regular (or "retail") advisory activities, which the Advisers Act and its rules are clearly designed to regulate.<sup>32</sup> Such an exception would be inconsistent with functional regulation principles.<sup>33</sup> A general exception would

an investment for a trust account for which it has [investment] discretion that presents a conflict of interest, but which applicable law authorizes, the trustee has not necessarily complied with the duty of prudence with respect to that investment." *Id.* OTS trust activities regulations generally prohibit a savings association exercising investment discretion over a fiduciary account from lending, selling or otherwise transferring fiduciary account assets if the savings association has an interest in the transaction. (12 CFR 550.350). Similarly, OTS regulations prohibit a savings association from investing funds of a discretionary fiduciary account in stock or obligations acquired from the savings association or its affiliates. (12 CFR 550.330). These regulations contain exceptions for transactions authorized by applicable law. However, applicable trust law generally contains very few exceptions permitting these types of conflict-of-interest transactions. *See, e.g.,* Bogert, *supra* note 14, at § 543; Scott, *supra* note 14, at §§ 170–170.24, 170.25.

<sup>31</sup> Exchange Act Release No. 44291, *supra* note 17, at 27788 ("Now that the general exception for banks has been replaced \* \* \* it seems reasonable to afford savings associations and savings banks the same type of exemptions."). Under this new exemption, thrifts' retail brokerage activities will be subject to the same limitations as banks'.

<sup>32</sup> OTS regulations include these retail activities within the OTS definition of "fiduciary capacities." 12 CFR 550.30. The OTS' definition establishes the scope of Part 550, which contains the OTS' rules governing a thrift's use of powers that the OTS has specially authorized the thrift to exercise under section 5(n) of the Home Owners' Loan Act (12 U.S.C. 1464(n)) and similar powers afforded the thrift under other applicable laws. *See* 12 CFR 550.20, 12 CFR 550.130, and 12 CFR 550.580. It is necessary, however, to look beyond these designations for purposes of our analysis of federal securities law and any exemption for thrifts under the Advisers Act.

<sup>33</sup> In this Release, we use "functional regulation" to mean "regulation of the same functions, or activities, by the same expert regulator, regardless of the nature of the entity engaging in those activities." H.R. Rep. No. 106–74, part 3, at 106th Cong., 1st Sess. at 113–14 (1999). The Commission has consistently and strongly supported functional regulation of all participants in the securities markets so that the same rules apply to the same activities. *See Concerning Financial Modernization and H.R. 10, The Financial Services Competition Act of 1997: Hearings Before the Subcommittee on Financial and Hazardous Materials, of the House of Representatives Committee on Commerce*, 105th Cong., 1st Sess. (July 17, 1997) (testimony of Arthur

also treat thrifts that provide retail advisory services differently from other registered advisers providing the same services, thus creating regulatory disparity for the firms and for their clients. Further, a general exception could result in many integrated financial services firms moving regular advisory activities to their captive thrifts in order to escape regulation under the Act.<sup>34</sup>

Most significantly, a general exception would eliminate important investor protections afforded to advisory clients under the Advisers Act. For example, investment advisers must provide clients and prospective clients with an informational brochure addressing certain conflict-of-interest issues and explaining the adviser's business practices, fees, investment policies and risks, brokerage practices (such as soft dollar usage), and industry affiliations, and must disclose their policies on voting proxies.<sup>35</sup> Investment advisers are also restricted with respect to the content of their advertisements and the types of advisory fees they charge.<sup>36</sup> A broad exception would eliminate these and other measures

Levitt, Chairman, U.S. Securities and Exchange Commission). *See also Concerning Financial Services Modernization and H.R. 192: Hearings Before the Subcommittee on Financial Institutions Supervision, Regulation and Insurance, of the House of Representatives Committee on Banking, Finance and Urban Affairs*, 102nd Cong., 1st Sess. (Feb. 28, 1991) (testimony of Richard C. Breeden, Chairman, U.S. Securities and Exchange Commission); *Concerning H.R. 1505, H.R. 6, and H.R. 15: Hearings Before the Subcommittee on Financial Institutions Supervision, Regulation and Insurance, of the House of Representatives Committee on Banking, Finance and Urban Affairs*, 102nd Cong., 1st Sess. (Apr. 30, 1991) (testimony of Richard C. Breeden, Chairman, U.S. Securities and Exchange Commission).

<sup>34</sup> As we discuss in section I.E. of this Release below, a number of financial services firms already operate subsidiaries with thrift charters.

<sup>35</sup> Rule 204–3 (15 CFR 275.204–3); Electronic Filing by Investment Advisers; Proposed Amendments to Form ADV, Investment Advisers Act Release No. 1862 (Apr. 5, 2000) (65 FR 20524 (Apr. 17, 2000)). Investment advisers must also disclose any disciplinary history to clients and prospective clients. Rule 206(4)–4 (15 CFR 275.206(4)–4). Any potential investor with questions about the disciplinary history or business of a registered investment advisor may access, free of charge, a Web-based database containing such information at <http://www.adviserinfo.sec.gov>.

<sup>36</sup> We have adopted a rule prohibiting a number of advertising practices. For example, an investment adviser's advertisement may not contain past specific investment recommendations unless the adviser lists all recommendations made during the previous year. Rule 206(4)–1(a)(2) (15 CFR 275.206(4)–1(a)(2)). With respect to advisory fees, Congress, out of a concern that performance-based fees would encourage undue speculation with client funds, enacted section 205 of the Advisers Act (15 U.S.C. 80b–5). Section 205 generally prohibits advisers from charging fees based on a share of the capital gains or capital appreciation of clients' funds.

under the Advisers Act that currently protect thrifts' retail advisory clients.<sup>37</sup>

We discuss the proposed rule and each of its provisions below.

#### A. Thrift Institutions Deemed Not To Be Investment Advisers

Proposed rule 202(a)(11)–2(a)(1) would except thrift institutions from the Advisers Act to the extent their investment advice is provided in their capacity as trustee, executor, administrator, or guardian for trusts, estates, guardianships and other accounts created and maintained for a fiduciary purpose, and they do not, except in connection with the ordinary advertising of their services as trustee, executor, administrator, or guardian for these fiduciary purpose accounts, hold themselves out generally to the public as providing investment advisory services.<sup>38</sup> Proposed rule 202(a)(11)–2(a)(2) would except a thrift institution from the Advisers Act to the extent its investment advice is provided to a collective trust fund maintained by the thrift institution and excepted from the definition of the term "investment company" under section 3(c)(1) of the Investment Company Act.<sup>39</sup> Thrifts that meet these conditions would be deemed not to be investment advisers, and thus not subject to any provisions of the Act.

#### 1. Eligible Thrift Institutions

Proposed rule 202(a)(11)–2 would be available to savings associations that have deposits insured by the FDIC.<sup>40</sup> These institutions include federal savings associations, federal savings banks, and state-chartered savings associations. Federal savings associations and federal savings banks are chartered and regulated by the OTS, which also oversees and monitors FDIC-insured state-chartered savings associations.<sup>41</sup> The requirement that the

<sup>37</sup> Advisory firm employees may also be subject to certain state testing and licensing requirements. An OTS regulation, however, asserts that state law regarding registration and licensing, apparently including investment adviser licensing requirements, is preempted with respect to thrifts' fiduciary activities. 12 CFR 550.136. *See* OTS Recordkeeping Rules Release, *supra* note 13.

<sup>38</sup> Proposed 202(a)(11)–2(a)(1).

<sup>39</sup> Proposed 202(a)(11)–2(a)(2). The rule would also cover the thrift to the extent it advises accounts whose assets are invested solely in the thrift's collective trust funds.

<sup>40</sup> Proposed rule 202(a)(11)–2(c). In the proposed rule, the term "thrift" covers "savings associations" as they are defined in section 3(b)(1) of the Federal Deposit Insurance Act (15 U.S.C. 1813(b)(1)). Thus, "thrift" includes any federal savings association or federal savings bank chartered under 12 U.S.C. 1464, and any state savings association.

<sup>41</sup> The Director of the OTS is charged with examination, safe and sound operation, and regulation of "savings associations." 12 U.S.C.

Continued

thrift be FDIC-insured is designed so that the thrifts relying on the rule will be overseen at the federal level.<sup>42</sup>

We request comment on the coverage of the proposed rule.

- Are any institutions excluded that should be included? Would it be useful to include state savings banks?
- Have we included any institutions that should be excluded?

## 2. Scope of the Rule

### a. Fiduciary Purpose Accounts

Proposed rule 202(a)(11)–2(a)(1) would except a thrift institution from the Advisers Act to the extent it performs advisory services solely in its capacity as trustee, executor, administrator, or guardian for trusts, estates, guardianships and other accounts created and established for a fiduciary purpose (rather than primarily for money management), provided the thrift does not hold itself out as providing investment advisory services.<sup>43</sup>

We have drafted these conditions so that only thrift advisory activities that are part of certain fiduciary activities, that have been provided by banks and are now also offered by thrifts, are excepted from the Advisers Act.<sup>44</sup> We have drawn the conditions from the Gramm-Leach-Bliley Act's amendments to the Investment Company Act that permit thrifts to operate common trust funds excepted from the definition of "investment company" under the Investment Company Act on the same basis as banks.<sup>45</sup> The Gramm-Leach-Bliley amendments also clarified that the scope of this "bank common trust

1463(a). For those purposes, "savings association" means a savings association, as defined in section 3 of the Federal Deposit Insurance Act, whose deposits are insured by the FDIC. 12 U.S.C. 1462(4). As OTS-chartered savings associations, all federal savings associations and federal savings banks must be FDIC-insured. See 12 CFR 543.2(g)(2)(i) and 12 CFR 552.2–1(b)(3)(i).

<sup>42</sup> We expect that nearly all state savings associations would meet this condition of the proposed rule.

Proposed rule 202(a)(11)–2 would not be available to thrifts operated for the purpose of evading the provisions of the Advisers Act. Proposed rule 202(a)(11)–2(c). This limitation is similar to section 208(d) of the Act, which makes it unlawful to do indirectly what one may not do directly. 15 U.S.C. 80b–8(d).

<sup>43</sup> Proposed rule 202(a)(11)–2(a)(1).

<sup>44</sup> The line we would draw in the proposed rule is similar to that suggested in an article by a former senior official at the OCC. Our proposed rule would except thrift trust department activities that the article describes as having "no real counterpart" in the securities business, while activities that are (or are very similar to activities that are) also performed by securities firms would remain subject to the Advisers Act. Dean Miller, *The Supervision of Bank Asset Management Activities*, Trusts & Estates, Mar. 1, 2000.

<sup>45</sup> See *supra* notes—and accompanying text.

fund exception" is limited to common trust funds that are operated solely as an aid to a bank's administration of trusts or other accounts maintained for a "bona fide" fiduciary purpose.<sup>46</sup>

Proposed rule 202(a)(11)–2(a)(1) would permit a thrift institution to provide advisory services *in its capacity as trustee, executor, administrator, or guardian for the customer account receiving the advice, without being subject to the Act*.<sup>48</sup> These are the same capacities in which a thrift must hold assets to place them in a common trust fund that is excepted from the definition of "investment company" under the Investment Company Act. In each case, the account advised by the thrift must be established and maintained *for a fiduciary purpose*.<sup>49</sup> This is the same

<sup>46</sup> As amended by the Gramm-Leach-Bliley Act, section 3(c)(3) excepts from the definition of "investment company" any common trust fund maintained by a bank exclusively for the collective investment of commingled trust assets held by the bank in its capacity as trustee, executor, administrator, or guardian "if—

(A) such fund is employed by the bank solely as an aid to the administration of trusts, estates, or other accounts created and maintained for a fiduciary purpose;

(B) except in connection with the ordinary advertising of the bank's fiduciary services, interests in such fund are not—

(i) advertised; or

(ii) offered for sale to the general public; and

(C) fees and expenses charged by such fund are not in contravention of fiduciary principles established under applicable Federal or State law." 15 U.S.C. 80a–3(c)(3).

Before it was amended by the Gramm-Leach-Bliley Act, section 3(c)(3) of the Investment Company Act excepted from the definition of "investment company" any common trust fund maintained by a bank exclusively for the collective investment of commingled trust assets held by the bank in its capacity as trustee, executor, administrator, or guardian. The staff of the Commission has long interpreted the scope of this exception to be limited to common trust funds that are operated solely as an aid to a bank's administration of trusts or other accounts maintained for a "bona fide" fiduciary purpose, and the staff has issued a number of interpretive letters explaining the types of accounts that have, or lack, a fiduciary purpose. See *infra* notes 53–56. Congress amended section 3(c)(3) in the Gramm-Leach-Bliley Act to codify this long-standing position. H.R. Rep. 106–74 (Pt. 3), 106th Cong., 1st Sess. 182 (1999).

<sup>47</sup> The OTS Trust Handbook explains that "[t]he person or entity named to settle an estate by the decedent's will is commonly referred to as the 'executor' of the decedent's estate. The person or entity named to settle an estate where no will exists is commonly referred to as the 'administrator' of the decedent's estate. Financial institutions are often appointed in these capacities." OTS Trust Handbook, *supra* note , at 100.2.

<sup>48</sup> Thrifts that serve trust accounts solely in other capacities would not qualify for the exception. For example, a thrift that is not the trustee for a trust, but is engaged by the trustee as custodian for the trust, could not also provide investment advice to that trust and still rely on the rule.

<sup>49</sup> A note to the proposed rule clarifies that the "fiduciary purpose" requirement applies to each account to which the thrift provides investment

requirement that a thrift must meet for each customer account included in a common trust fund excepted from the Investment Company Act.<sup>50</sup>

To meet the "fiduciary purpose" requirement, the customer account must be established and maintained for an underlying fiduciary reason. A customer account established primarily for money management reasons lacks an underlying fiduciary purpose and cannot meet this requirement.<sup>51</sup> Thus, "fiduciary purpose accounts" would include those established in connection with estate planning, conservatorships and guardianships,<sup>52</sup> and those established for minors under the Uniform Gifts to Minors Act ("UGMA").<sup>53</sup> Accounts established primarily for money management, custodial or administrative purposes, e.g., managed agency accounts,<sup>54</sup> individual retirement account (IRA) trusts,<sup>55</sup> indenture trusts, college

advisory services, whether that account takes the form of a trust, an estate, a guardianship or another type of account.

<sup>50</sup> Not all trust department accounts, or even all trusts, necessarily have a fiduciary purpose. Whether a customer establishes a trust, or other account, for a fiduciary purpose depends not only on the terms of the trust instrument (or other documents setting up the account), but also on other facts and circumstances concerning the creation and use of the account. Cf. *United Missouri Bank of Kansas City, N.A.*, SEC Staff No-Action Letter (Dec. 31, 1981) (citing 26 Fed. Reserve Bull. 394 (1940), in which the Federal Reserve Board expressed views that formed the original basis for the Investment Company Act common trust fund exception).

<sup>51</sup> Whether the customer account has a fiduciary purpose is distinct from whether the thrift acts in a fiduciary capacity with respect to the account. All investment advisers act in a fiduciary capacity for their clients and therefore owe fiduciary duties to their clients, see *Capital Gains, supra* note 2, but the fiduciary obligations of the adviser do not mean that the client's portfolio was established for a fiduciary purpose.

<sup>52</sup> Section 3(c)(3) of the Investment Company Act refers to "trusts, estates, or other accounts created and maintained for a fiduciary purpose" but does not expressly mention guardianships. 15 U.S.C. 80a–3(c)(3). To provide further clarification to thrifts, proposed rule 202(a)(11)–2(a)(1) specifically refers to guardianships.

<sup>53</sup> The Commission's staff has provided clarification, through no-action letters, as to the fiduciary purposes that qualify an account to be pooled under the common trust fund exception in section 3(c)(3) of the Investment Company Act. See e.g., *Commercial Bank*, SEC Staff No-Action Letter (Feb. 24, 1988) (traditional estate planning); *Texas Commerce Bank Nat'l Association*, SEC Staff No-Action Letter (Jan. 26, 1978) (UGMA).

<sup>54</sup> A managed agency account would not be included under the proposed exception even if the underlying assets are held in a trust established for a fiduciary purpose. The thrift, like most other investment advisers that manage trusts' assets, would be acting as agent rather than as trustee, executor, administrator or guardian.

<sup>55</sup> The common trust fund holding IRA assets because such assets are not held "for a fiduciary purpose." Exchange Act Release No.

savings trusts, ERISA trusts, "rabbi" trusts, and most revocable inter-vivos trusts, would not be included under rule 202(a)(11)–2(a)(1).<sup>56</sup>

A thrift institution relying on proposed rule 202(a)(11)–2(a)(1) could not hold itself out generally to the public as providing investment advisory services. Advertising or otherwise holding itself out as providing investment advice, portfolio management services, or financial planning would not be consistent with the proposed rule's requirement that the thrift's advisory services be solely in its capacity as trustee, executor, administrator, or guardian. Under the proposed rule, however, a thrift institution could publicize its investment advisory services in connection with the ordinary advertising of its services as trustee, executor, administrator, or guardian to fiduciary purpose accounts.<sup>57</sup>

We request comment on the scope of this proposed exception.

44291, *supra* note 17, at note 85. Some banks have suggested to our Division of Investment Management that, based on a letter from that Division, their common trust funds should be permitted to hold IRA assets and qualify for the exception. See *Continental Bank*, SEC Staff No-Action Letter (Sep. 2, 1982). The amendments to section 3(c)(3) effected by the Gramm-Leach-Bliley Act, however, codify our longstanding interpretation that a bank common trust fund cannot qualify for the exception if it holds assets of accounts that lack fiduciary purpose, including IRAs. See *Concerning H.R. 1505, H.R. 6, and H.R. 15: Hearings Before the Subcommittee on Financial Institutions Supervision, Regulation and Insurance, of the House of Representatives Committee on Banking, Finance and Urban Affairs*, 102nd Cong., 1st Sess. (Apr. 30, 1991) (testimony of Richard C. Breen, Chairman, U.S. Securities and Exchange Commission). Cf. *Santa Barbara Bank & Trust*, *supra* note 46 (stating that the Commission and its staff have determined that the exception is not available for common trust funds holding assets of IRAs).

<sup>56</sup> The staff has issued letters explaining that "rabbi" trusts are not created for a fiduciary purpose, since they are a means for an employer to provide deferred compensation to top executives. See e.g., *Boatmen's Bancshares, Inc.*, SEC Staff No-Action Letter (Aug. 17, 1994). The staff has also issued guidance that revocable inter vivos trusts generally do not have a fiduciary purpose because grantors of these trusts usually retain so much control over the trust that it appears to be merely a vehicle for money management. However, a trust that can show that it has a true fiduciary purpose can rebut this presumption. See, e.g., *First Jersey National Bank*, SEC Staff No-Action Letter (Nov. 13, 1987); *Provident National Bank Middle Market Trust Program*, SEC Staff No-Action Letter (Feb. 17, 1982); *Genesee Merchants Bank and Trust*, SEC Staff No-Action Letter (Jan. 8, 1979).

<sup>57</sup> Therefore, except to the extent that a federal thrift relying on the proposed rule is advertising the services it provides to such fiduciary purpose accounts, it may not publicly represent itself as an investment adviser or as providing investment advisory services. The proposed limitation on advertising again parallels Congress' revisions, in the Gramm-Leach-Bliley Act, to section 3(c)(3) of the Investment Company Act. See *supra* note 46.

• With respect to trust accounts, should we be guided by revised section 3(c)(3) of the Investment Company Act? We request that commenters disagreeing with our approach provide alternatives.

• Are the rule's limitations clear? If not, we urge commenters to suggest additional guidance that we could provide to clarify the "fiduciary purpose" requirement. We specifically request comments on whether there are fiduciary roles that thrifts typically play, other than acting as trustee, executor, administrator, or guardian, that have no real counterpart in regular investment advisory firms, but that would require the thrift to provide investment advisory services.

• Should the rule permit thrifts to advise managed agency accounts that have a fiduciary purpose without being subject to the Act? Trustees of fiduciary purpose accounts often hire a thrift or other registered investment adviser, as an agent, to manage the trust's assets, and the adviser treats the trustee as its client for purposes of disclosure and consent. Should thrifts be exempt with respect to fiduciary purpose accounts for which they act as agent, but not as trustee, executor, administrator or guardian?

• We also ask that commenters who oppose the exception or who believe it to be too broad suggest appropriate means for thrifts to comply with the Advisers Act when acting as both adviser and trustee for the types of fiduciary accounts that would meet the requirements of the proposed rule. For example, to whom should the thrift send its informational brochure or other disclosure when it acts as guardian for an incompetent, or as trustee under a testamentary trust that benefits minor children?

#### b. Collective Trust Fund Accounts

Proposed rule 202(a)(11)–2(a)(2) would except a thrift institution from the Advisers Act to the extent it provides investment advisory services to its collective trust funds that are excepted from the definition of "investment company" under the Investment Company Act. Collective trust funds allow a bank or thrift to manage the assets of tax-qualified pension and profit sharing plans on a pooled basis without creating an "investment company."<sup>58</sup> The Investment Company Act has excepted banks' collective trust funds from the definition of "investment company"

<sup>58</sup> Thrift-sponsored collective trust funds are excepted from the definition of the term "investment company" under section 3(c)(11) of the Investment Company Act. 15 U.S.C. 80a–3(c)(11).

since 1970,<sup>59</sup> and in the Gramm-Leach-Bliley Act Congress extended this exception to collective trust funds maintained by thrifts.

Consistent with Congress' extension of the Investment Company Act collective trust fund exception, we are proposing to except thrifts from the Advisers Act to the extent they provide investment advice to their collective trust funds excepted from the definition of "investment company."<sup>60</sup> In addition, our proposed rule would except a thrift from the Advisers Act with respect to accounts invested solely in one or more of the thrift's sponsored collective trust funds.

• Should we be guided by Congress' decision to exempt thrift-sponsored collective trust funds from the Investment Company Act?

• Should thrifts also be excepted from the Advisers Act with respect to the separate accounts of employee benefit plans whose assets are pooled in the collective trust account?

#### B. Thrift Institutions Registered Under the Act

Many thrifts may be required to maintain their existing registrations as investment advisers under the Act, even if we adopt the rule that we are today proposing, because of the scope of their advisory business or marketing activities. For these registered thrifts, our proposed rule includes a paragraph clarifying that we would not necessarily apply the Act to all of the thrift's customer relationships. Under the rule, so long as the thrift makes the undertaking described below, the Advisers Act would apply to the thrift institution only with respect to those customer accounts for which the thrift provides advisory services that subject it to the Act.<sup>61</sup> For example, the Advisers Act would apply to the thrift institution when it advises managed agency accounts or IRA trusts, but may not apply to the same thrift when it serves as trustee to a testamentary trust.

To qualify for this provision of proposed rule 202(a)(11)–2, a thrift

<sup>59</sup> Investment Company Amendments Act of 1970, Pub. L. No. 91–547, section 3(b)(5), 84 Stat. 1415.

<sup>60</sup> We are also proposing a conforming rule under the Exchange Act, to exempt thrift-sponsored collective trust funds from the requirements of section 12 of that Act. See Section I.D. of this Release, *infra*.

<sup>61</sup> Proposed rule 202(a)(11)–2(b). This is the same approach we have taken in applying the Act to firms registered under both the Exchange Act (as a broker) and the Advisers Act (as an adviser), and that we have proposed to codify in a rule. Certain Broker-Dealers Deemed Not To Be Investment Advisers, Advisers Act Release No. 1845 (Nov. 4, 1999) [64 FR 61226 (Nov. 10, 1999)] ("Advisers Act Broker-Dealer Proposal").

institution registered with us as an adviser would be required to confirm that it will provide us with access to all of its trust department records.<sup>62</sup> Under section 204 of the Advisers Act, all records of any investment adviser, including a thrift institution that provides advisory services, are already subject to examination by Commission representatives.<sup>63</sup> Continued access to these records will permit us to determine whether the thrift institution has defrauded advisory clients, for example, by failing to disclose misallocations of initial public offerings or other trades in favor of other trust department clients.<sup>64</sup> These records are considered examination records, and thus receive the confidentiality available under section 210(b) of the Advisers Act.<sup>65</sup>

### C. Amendment To Form ADV

We are proposing minor amendments to Form ADV and its instructions to identify those registered investment advisers that are thrift institutions.<sup>66</sup> Form ADV, the investment adviser registration form, currently asks whether the adviser is actively engaged in business as a bank.<sup>67</sup> We propose to amend the Form also to ask whether the adviser is actively engaged in business as a thrift institution. We believe this information would be necessary to allow us to enforce the conditions of proposed rule 202(a)(11)–2(b), if adopted.

### D. Exemption Under Securities Exchange Act

We are proposing new rule 12g–6 under the Exchange Act, to exempt thrift-sponsored collective trust funds from the registration and reporting

requirements of the Exchange Act. As discussed above, the Gramm-Leach-Bliley Act amended the Investment Company Act to exempt thrift-sponsored common trust funds and thrift-sponsored collective trust funds from the definition of “investment company.” Like bank common trust funds, thrift-sponsored common trust funds are exempt from the Exchange Act.<sup>68</sup> However, the provision exempting bank collective trust funds from the Exchange Act does not extend to thrifts.<sup>69</sup> We believe that exempting thrifts’ collective trust funds from the Exchange Act is consistent with Congress’ determination in the Gramm-Leach-Bliley Act to exempt those collective trust funds from the Investment Company Act. We request comment on the scope of this proposed exemption.

### E. Effects on Competition

Based on our general understanding of the types of clients served by the trust departments of thrift institutions, we believe the proposed rule would have the effect of eliminating certain regulatory disparities between banks and thrifts that carry on a fiduciary trust business, without creating new regulatory disparities between thrifts and regular investment advisory firms. We are requesting comment on our understanding of the thrift industry in this regard.

There are approximately 932 insured savings associations in operation. Of these, only 117 savings associations were authorized to establish trust departments, and even fewer—98—filed regulatory reports indicating that they administer any assets pursuant to their trust powers.<sup>70</sup> We estimate that approximately 34 savings associations are registered with us as investment advisers.<sup>71</sup>

Nineteen of the savings associations registered with us as investment advisers are part of national or regional securities or insurance firm complexes in which a number of different types of regulated firms carry out various roles in order to provide a broad selection of financial services and products. With limited exception, the savings associations in these large firms do not appear to engage in any appreciable lending or deposit-taking.<sup>72</sup> Eight of these large firms appear to use their savings associations predominantly to provide services to clients seeking agency accounts or employee benefit trust accounts such as IRAs or ERISA plan accounts, which, under the proposed rule, would not have a fiduciary purpose.<sup>73</sup> Eleven of these large firms may be using, to varying extents, their savings associations to provide fiduciary services to clients in connection with trusts, estates, guardianships and other accounts created and maintained for a fiduciary purpose.<sup>74</sup> However, total trust assets reported by the former group far exceeds that of the latter.<sup>75</sup>

203A(a) of the Advisers Act (15 U.S.C. 80b–3A(a)). Section 203A(a) generally prohibits an investment adviser from registering with the Commission unless the adviser is providing continuous and regular supervisory or management services for at least \$25 million of client assets or advises a registered investment company.

<sup>72</sup> Our staff reviewed asset and liability data for all 34 savings associations. The data were reported by these savings associations in their September 30, 2003 Thrift Financial Reports (TFRs), and summarized at [http://www2.fdic.gov/idasprpt\\_financial.asp](http://www2.fdic.gov/idasprpt_financial.asp) (visited Jan. 27, 2004). Of the 19 savings associations that are part of large firms, 15 reported only nominal lending or deposit-taking activity. Three others reported lending activity, but only two reported loan assets that exceeded trust assets, whereas loan assets for the other one were small in relation to its trust assets. The one remaining savings association in the group reported no lending activity and deposits equaling approximately 11% of trust assets, comprised mainly of uninsured jumbo deposits.

<sup>73</sup> Our staff reviewed trust department data for all 34 savings associations. The data were reported by these savings associations in their September 30, 2003 TFRs (available at [http://www2.fdic.gov/call\\_tfr\\_rpts/?catNumber=74](http://www2.fdic.gov/call_tfr_rpts/?catNumber=74) (visited Jan. 27, 2004)).

<sup>74</sup> The TFR contains a separate category for personal trust accounts, but it does not require the institution to report fiduciary-purpose trust accounts separately from other personal trust accounts. For purposes of this analysis, our staff treated all managed personal trust accounts as fiduciary accounts, although this approach likely overestimates the number of fiduciary accounts. For five of these eleven savings associations, the total reported assets for managed personal trust accounts was approximately 25% to 45% of the total trust assets reported by the savings association, and was approximately 50% or more for the other six savings associations in this group of eleven. In comparison, the same figures for the group of eight large firms that focus primarily on non-fiduciary accounts ranged from less than 1% to 16%.

<sup>75</sup> The eight large firms that focus primarily on non-fiduciary accounts reported trust assets totaling approximately \$97.4 billion, whereas the eleven

<sup>62</sup> The thrift would effect this through an undertaking in its Form ADV (Schedule D, Miscellaneous Section). The undertaking need not be complex; it could state simply that the thrift undertakes to provide the Commission with access to all trust department records.

<sup>63</sup> Section 204 of the Advisers Act (15 U.S.C. 80b–4) applies to all investment advisers using interstate commerce in connection with their business, other than advisers specifically exempted from registration pursuant to section 203(b) (15 U.S.C. 80b–3(b)).

<sup>64</sup> See *In the Matter of F.W. Thompson*, Investment Advisers Act Release No. 1895, 73 S.E.C. Docket 486 (Sept. 7, 2000) (adviser failed to disclose inequitable method of allocating IPO shares, which disproportionately favored certain clients to the detriment of others); *In the Matter of McKenzie Walker Investment Management, Inc. and Richard C. McKenzie, Jr.*, Investment Advisers Act Release No. 1571, 62 S.E.C. Docket 1010 (July 16, 1996) (adviser unlawfully failed to disclose its practice of favorably allocating IPO and other equity trades to performance-fee paying clients over its other clients).

<sup>65</sup> 15 U.S.C. 80b–10(b).

<sup>66</sup> 17 CFR 279.1.

<sup>67</sup> Item 6.A(6) of Part 1A of Form ADV.

<sup>68</sup> Section 3(a)(12)(A)(iii) of the Exchange Act [15 U.S.C. 78c(a)(12)(A)(iii)].

<sup>69</sup> Section 3(a)(12)(A)(iv) of the Exchange Act [15 U.S.C. 78c(a)(12)(A)(iv)].

<sup>70</sup> These estimates are as of September 30, 2003. We base them on our staff’s review of data on all U.S. insured depository institutions, maintained by the Federal Deposit Insurance Corporation (FDIC) and made available at <http://www2.fdic.gov/idasprmain> (visited Jan. 23, 2004) and [http://www2.fdic.gov/sdirpt\\_Financial.asp](http://www2.fdic.gov/sdirpt_Financial.asp) (visited Jan. 26, 2004).

<sup>71</sup> We base this estimate on our staff’s review of our adviser registration records to find any of the names of the 117 savings associations identified by FDIC data as having trust powers (at <http://www2.fdic.gov/idasprmain> (visited Jan. 23, 2004)). We cannot precisely determine the number of thrifts registered with us because we do not currently require registered investment advisers to indicate on Form ADV whether they possess a thrift charter. We infer that the remaining 64 savings associations are not registered with us because they are ineligible to do so, as provided by section



The other 15 savings associations registered with us appear to function as depository institutions, focused primarily on lending and deposit-taking, and are not business units of national or regional securities or insurance firms.<sup>76</sup> Four of these depository-institution savings associations appear to use their trust departments predominantly to provide services to clients seeking agency accounts and employee benefit trust accounts such as IRAs or ERISA plan accounts, which, under the proposed rule, would not have a fiduciary purpose.<sup>77</sup> The remaining 11 of these depository-institution savings associations may be using, to varying extents, their trust departments to provide fiduciary services to clients in connection with trusts, estates, guardianships and other accounts created and maintained for a fiduciary purpose.<sup>78</sup> Total trust assets reported by the 11 depository institution savings associations providing a greater proportion of fiduciary account services far exceed the total trust assets reported by the four focusing on non-fiduciary accounts.<sup>79</sup>

The above data lead us to infer that, for the savings associations registered with us that use a lending and deposit-taking business model in competition with banks, the savings associations with the majority of the trust business may be holding significant proportions of their total trust assets in fiduciary purpose accounts. By excepting thrift institutions from the Advisers Act to the extent they provide investment advice

firms that provide services to a greater proportion of fiduciary accounts reported trust assets totaling only \$8.5 billion.

<sup>76</sup> One of these depository-institution savings associations reports loan assets in excess of \$15 billion on its September 30, 2003 TFR and is part of a world-wide financial holding company. Seven others appear to be regional institutions, reporting loan assets in the range of approximately \$1.4 billion to \$10.8 billion on their September 30, 2003 TFR. Two others, reporting loan assets of approximately \$380 million and \$140 million respectively, are affiliated with regional financial holding companies. The remaining five depository-institution savings associations are smaller, reporting approximately \$78 million to \$650 million in loan assets.

<sup>77</sup> Each of these four savings associations reported that less than 15% of its total trust assets were held in managed personal trust accounts.

<sup>78</sup> Five of these eleven savings associations each reported that approximately 20% to 25% of its total trust assets were held in managed personal trust accounts. The remaining six savings associations each reported that approximately 35% to 85% of its total trust assets were held in managed personal trust accounts.

<sup>79</sup> The 11 depository-institution savings associations that provide fiduciary accounts reported trust assets totaling approximately \$13.1 billion, whereas the four depository-institution savings associations that focus primarily on non-fiduciary accounts reported trust assets totaling approximately \$940 million.

in their capacity as trustee, executor, administrator, or guardian for accounts with an underlying fiduciary purpose, proposed rule 202(a)(11)-2 will eliminate an existing regulatory disparity between banks and these savings associations. In addition, it is our understanding that the category of thrift customer relationships that the proposed rule would affect—that is, fiduciary purpose trust customers—is not commonly served by regular investment advisory firms. Thus, the proposed rule will not create regulatory disparities between thrifts and regular investment advisory firms.

On the other hand, the above data also lead us to infer that the vast majority of trust business conducted by all the savings associations registered with us is carried on by savings associations that are part of securities and insurance firms, that do not use a lending and deposit-taking business model in competition with banks, and that do not hold significant proportions of their trust assets in fiduciary purpose accounts. Thus, a blanket exception for thrifts from the Advisers Act would be likely to create a new regulatory disparity between the majority of savings associations engaged in significant levels of advisory activity and the regular investment advisory firms with which they currently compete. Regular investment advisory firms would continue to be subject to the investor protection requirements under the Advisers Act, whereas savings associations that are part of large firms holding the dominant share of trust department assets (as discussed above) would be exempted from the same investor protection requirements, notwithstanding that they all appear to service the same types of clients.<sup>80</sup>

The proposed rule would not alter whatever competitive effects are caused by the existing regulatory disparity between savings associations that are part of large firms and banks. However, the existence and extent of any

<sup>80</sup> It appears unlikely that our proposed exemption for thrifts that hold trust assets in collective trust funds will create any competitive disparity for regular investment advisory firms. Our staff's review of TFR data shows that, at most, one or two of the 34 savings associations registered with us may presently be using collective trust funds. In addition, few of these thrifts managed employee benefit plan assets eligible for inclusion in a collective trust fund. Such assets reported by all 34 savings associations totaled approximately one percent of the aggregate trust assets administered by these savings associations. Only three, smaller savings associations out of the 34 registrants reported sizeable proportional holdings of these trust assets, in the range of 55%-65%. Four other savings associations out of the 34 registrants reported proportional holdings of these assets in the range of 10% to 12%, whereas the remaining 27 reported nothing more than nominal holdings.

competitive effects is dependent upon other factors as well. For example, there may be few or no competitive effects if banks are not presently seeking to provide the same types of retail investment advisory services as are being provided by these savings associations. Even if banks are providing the same types of retail investment advisory services, there may be no competitive effects if banks seek to provide these services primarily to their depository institution customer base as an accommodation.<sup>81</sup> This issue also raises a question as to whether the existing regulatory disparities are truly between banks and thrifts, or can more accurately be described as being between banks and the financial services complexes of which the thrifts are part.

We request comment on the following questions:

- Is our understanding of the nature and scope of investment advisory services provided by various types of thrifts correct?
- How many of these thrifts compete with banks for the same type of client?
- Do regular investment advisory firms compete, to any appreciable degree, with thrifts for fiduciary-purpose trust clients?

## II. General Request for Comment

Any interested persons wishing to submit written comments on the proposed rules that are the subject of this release, or to suggest additional changes or submit comments on other matters that might have an effect on the proposal described above, are requested to do so. Commenters suggesting alternative approaches are encouraged to submit proposed rule text.

For purposes of the Small Business Regulatory Enforcement Fairness Act of 1996, the Commission also is requesting information regarding the potential impact of the proposed rule on the economy on an annual basis. Commenters should provide empirical data to support their views.

## III. Cost-Benefit Analysis

### A. Background

Under proposed rule 202(a)(11)-2, certain thrifts would be deemed not to be "investment advisers" as defined in the Advisers Act when they render investment advice solely in their capacity as trustee, executor,

<sup>81</sup> In addition, any particular bank that also provides investment advice to a registered investment company—such as the bank's proprietary mutual funds—is now required to register under the Advisers Act on account of that activity. See *supra* note 7.

administrator, or guardian to customer accounts created and maintained for a fiduciary purpose, or when they advise collective trust funds they maintain under an exemption from the Investment Company Act.

The Commission is sensitive to the costs and benefits of its rules. We estimate that the proposed amendments may result in benefits to certain thrifts in the form of reduced regulatory compliance costs. As we discussed above, we estimate that approximately 34 thrifts are currently registered with us as investment advisers and incurring compliance costs that would be partially reduced by the proposed rule.<sup>82</sup> The extent of these cost reductions would depend on whether these thrifts continue using their trust departments primarily to provide retail investment advisory services.<sup>83</sup> Other thrifts that wish to begin operating trust departments under a business model that focuses exclusively on activities that would be covered by the proposed rule would obtain the benefit of complete avoidance of these compliance costs. We believe all these benefits can be obtained without imposing any significant costs on thrifts or investors.

### B. Benefits

#### 1. Complete Avoidance of Registration and Compliance Costs

To the extent their trust department activities fit within the activities identified in the proposed rule, thrifts will benefit in the form of saved costs they would otherwise expend in connection with Advisers Act compliance. Based on our staff's review of regulatory reports filed by SEC-registered thrifts describing their trust department activities, it appears that few, if any, currently engage exclusively in the type of fiduciary-purpose activities that would be exempted by proposed rule 202(a)(11)-(2)(a)(1). All but one or two of the 34 savings associations currently registered with us

<sup>82</sup> We estimate that approximately 34 savings associations have registered with us as investment advisers, based on our staff's review of SEC-registered investment advisers whose names identify them as savings associations. See *supra* note 71.

<sup>83</sup> Our staff reviewed data from savings associations that are registered with us as investment advisers that they reported in their September 30, 2003 Thrift Financial Reports (TFRs). A few of the 34 savings associations held all or nearly all their trust assets in personal trust accounts, but most of the 34 savings associations held most of their trust assets, or significant portions of them, in other types of accounts that would not meet the requirements of the proposed rule. More than half of the 34 savings associations were part of national or regional securities or insurance complexes. See *supra* notes 73, 74, 77, and 78.

as investment advisers report to the OTS that some or all of their trust assets are held in connection with non-fiduciary agency accounts or non-fiduciary employee benefit trust accounts such as IRAs or participant-directed 401(k) plans.<sup>84</sup> Thrift institutions operating under proposed rule 202(a)(11)-2(a)(2) could also save compliance costs associated with trust assets they manage for certain employee benefit plans through collective trust funds. They could also save the costs of registration and reporting required under the Exchange Act for those collective trust funds, under our proposed rule 12g-6 under the Exchange Act. However, it appears that few, if any, of the 34 currently-registered thrifts use collective trust funds. Moreover, few of them manage more than a nominal amount of employee benefit plan assets that would be eligible for inclusion in a collective trust fund.<sup>85</sup>

Benefits under proposed rule 202(a)(11)-2(a)(1) and (2) would be greater for thrifts that choose to operate their trust departments under a business model that focused exclusively on the types of accounts excepted under the proposed rule. Based on our staff's discussions with thrift industry representatives, we believe certain thrifts wish to establish or expand trust department operations using this business model, but we do not have sufficient information to estimate the number or size of such thrifts. These thrifts would be excepted from the requirement to file their registration statement on Form ADV and to pay filing fees to the operator of the IARD system that range from \$800 to \$1,100 initially and \$400 to \$550 annually.<sup>86</sup> For Paperwork Reduction Act ("PRA") purposes, the Commission further

<sup>84</sup> See *supra* notes 73, 74, 77, and 78.

<sup>85</sup> Based on our staff's review of September 30, 2003 TFR data, employee benefit plan assets that may be eligible for inclusion in a collective trust fund totaled less than one percent of the aggregate trust assets administered by the 34 savings associations currently registered with us. Only three smaller savings associations out of the 34 registrants reported sizeable proportional holdings of these trust assets, in the range of 55%-65%. Four other savings associations out of the 34 registrants reported proportional holdings of these assets in the range of 10% to 12%, whereas the remaining 27 reported nothing more than nominal holdings. See *supra* note 80.

<sup>86</sup> Registered advisers with assets under management of more than \$100 million must pay an initial set-up fee of \$1,100 and an annual updating fee of \$550. Advisers with assets under management of \$25 million to \$100 million must pay an initial set-up fee of \$800 and an annual updating fee of \$400. Other advisers, with assets under management of less than \$25 million, must pay an initial set-up fee of \$150 and an annual updating fee of \$100. See Investment Advisers Act Release No. 1888 (July 28, 2000) (65 FR 47807 (Aug. 3, 2000)) ("Advisers Act Release No. 1888").

estimates that the burden of completing and filing Form ADV for a new registrant is approximately 22 hours, and approximately 1.13 additional hours each year for annual amendments.<sup>87</sup> These thrifts would also save the cost of staff time expended in responding to questions and supplying records requested by our examiners during periodic exams.

Additionally, thrifts that operated under a business model that focuses exclusively on accounts exempted under the proposed rule would save costs associated with establishing and maintaining internal procedures and systems for complying with the Advisers Act and the rules under the Advisers Act. In connection with adopting our recent rules concerning investment adviser compliance programs, we estimated for Paperwork Reduction Act purposes that the average annual burden of these compliance programs is 80 hours.<sup>88</sup> However, given the systems and records these thrifts would still be required to maintain to comply with OTS requirements governing trust department activities, it is difficult to estimate whether these thrifts would obtain any marginal cost or burden decrease.

#### 2. Partial Avoidance of Costs

For most of the 34 thrifts currently registered with us, the proposed rule offers benefits in the form of saved compliance costs for that portion of their operations that manages trust assets held in fiduciary-purpose trust accounts. The proposed rule would include a paragraph clarifying that a thrift's obligations under the Advisers Act extend only to those customer accounts for which the thrift provides advisory services that subject it to the Act.<sup>89</sup>

Our staff has reviewed the trust department activities of the thrifts currently registered with us as investment advisers to identify the proportion of assets and accounts that may have lower compliance costs because they qualify for the proposed exception. The proportion of potentially-exempt assets in each thrift appears to vary across a range, from approximately 0.5 to 15 percent for 12

<sup>87</sup> The Commission has previously estimated a burden of approximately 0.75 hours per adviser per amendment filed on IARD. Currently registered advisers are estimated to amend their Form ADV, on average, 1.5 times per year. See Advisers Act Release No. 1888.

<sup>88</sup> Compliance Programs of Investment Companies and Investment Advisers, Investment Advisers Act Release No. 2204 (Dec. 17, 2003) [68 FR 74714 (Dec. 24, 2003)].

<sup>89</sup> Proposed rule 202(a)(11)-2(b). See *supra* Section I.B. of this Release.

of the thrifts at the low end, up to 50 to 100 percent for nine thrifts at the high end.<sup>90</sup> For the group, we estimate trust assets that may qualify for the fiduciary-purpose exception total approximately \$17.5 billion, or approximately 15% of the \$119 billion in total trust assets reported by the group.<sup>91</sup> For the exempt accounts containing these assets, these thrifts would save the cost of making client disclosures required under the Advisers Act.<sup>92</sup> These thrifts would also save the costs associated with other requirements under the Act and its rules relating to matters such as recordkeeping, custody, proxy voting on behalf of customers, and the like. While we use the percentage of a thrift trust department's assets held in potentially fiduciary-purpose accounts to describe, in relative terms, the proportion of these thrifts' exempt activities, their relative

cost savings would not necessarily vary by the same proportions. For a given amount of trust assets, a savings association's compliance costs may vary depending on the number of clients, their investment objectives, the type and turnover rate of the assets, the savings association's other securities activities, or even the personal activities of its trust department employees.

3. Competitive Effect Costs

The proposed rule would also benefit some of the 34 thrifts registered with us by eliminating certain regulatory disparities between banks and thrifts that carry on a fiduciary-purpose trust business covered by the proposed rule. This benefit is difficult to quantify. Other parties interested in this issue have suggested these regulatory disparities can be eliminated only by giving thrifts a blanket exemption from

the Advisers Act.<sup>93</sup> However, our review of registered thrifts shows this is unnecessary and would primarily create new regulatory disparities benefiting thrifts competing with other securities firms for retail advisory business.

As discussed above, our staff has reviewed the trust department activities of the thrifts currently registered with us as investment advisers. Based on this review, we infer that the vast majority of the trust activities conducted by thrifts, overall, are conducted by thrifts that are part of securities and insurance firms, that do not use a lending and deposit-taking business model in competition with banks, and that do not hold significant proportions of their trust assets in fiduciary purpose accounts. The following table summarizes these firms by business model.<sup>94</sup>

Category of thrift institution	Aggregate trust assets held by thrifts in the category (in billions)	Number of thrift institutions in category
Thrift Arms of Securities or Insurance Firms Using Retail Advisory Model .....	\$97.4	8
Thrift Arms of Securities or Insurance Firms with Significant Fiduciary-Purpose Accounts .....	8.5	11
Deposit-and-Lending Thrifts Using Retail Advisory Model .....	0.9	4
Deposit-and-Lending Thrifts with Significant Fiduciary-Purpose Accounts .....	13.1	11

This table shows that 15 of the 34 SEC-registered thrifts engage in a deposit-taking and lending business model in competition with banks. Eleven of these thrifts that compete with banks may be holding significant portions of their trust assets in fiduciary-purpose accounts, and the proposed rule would eliminate an existing regulatory disparity between these thrifts and banks. However, most of the trust business carried on by the 34 SEC-registered thrifts is being conducted by 8 thrifts using the retail advisory model that are part of a securities or insurance complex. Creating a blanket exception would create a new regulatory disparity between these thrifts and the regular investment advisory firms with which they currently compete.

C. Costs

We expect that a thrift relying on the proposed amendments would incur only minimal incremental costs. Thrifts

that would be required to maintain their Advisers Act registration and that could take advantage of the rule only with respect to certain accounts would be required to confirm, by including an undertaking in their Form ADV (Schedule D), that they will make all trust department records available to Commission examiners upon request. For PRA purposes, the Commission estimates that including this undertaking would impose an annual burden of only five minutes per thrift, or less than 10 hours in the aggregate.<sup>95</sup> Thrifts maintaining their registration under the Advisers Act would also be required to check a box on their Form ADV to indicate that they are actively engaged in business as a thrift institution. For PRA purposes, the Commission estimates that completing this item on Form ADV would impose an annual burden of only two minutes per thrift, or less than four hours in the aggregate.<sup>96</sup>

Costs to customers that receive investment advice from a thrift are also expected to be minimal. Customers whose accounts no longer subject the thrift to the Advisers Act will not receive the benefits and protections of the Act, including the disclosure that the Act requires. As discussed earlier, however, the Advisers Act does not work well when applied to certain thrift trust department relationships, and thus the benefits of the Act in these circumstances may already be minimal. Accordingly, we estimate the cost of removing the Act's benefits and protections with regard to these accounts would also be minimal, although those costs cannot be quantified.<sup>97</sup>

- The Commission requests comments on the costs and benefits identified in this release, as well as any other cost and benefits that may result from the proposal.
- We encourage commenters to identify, discuss, analyze, and supply

<sup>90</sup>This information was obtained from data reported by the 34 savings associations registered with us in their September 30, 2003 TFRs. See *supra* notes 73, 74, 75, and 77-79.

<sup>91</sup>*Id.*

<sup>92</sup>Investment advisers are required to deliver an information brochure to clients and prospective clients under rule 204-3 (17 CFR 275.204-3), and

to make detailed disclosures about the disciplinary history of the advisory firm and its supervised persons under rule 206(4)-4 (17 CFR 275.206(4)-4). The Commission has previously estimated that the annual burden of compliance with the brochure delivery requirements of rule 204-3 is approximately 694 hours per adviser, and that the annual burden of compliance with the disclosure

requirements of rule 206(4)-4 is 7.5 hours per adviser affected by rule 206(4)-4.

<sup>93</sup> See *supra* note and accompanying text.

<sup>94</sup>This table summarizes information presented in Section I.E. of this Release, *supra*.

<sup>95</sup> See *infra* note 101.

<sup>96</sup> See *infra* note 103.

<sup>97</sup> See *supra* note 27 and accompanying text.

empirical data relating to any costs and benefits they discuss.

- How many thrifts would qualify to use the proposed exceptions from the Advisers Act or from section 12(g) of the Exchange Act, and to what extent?
- Would the incremental costs saved by thrifts that were completely excepted from the Advisers Act be more than the cost savings for thrifts that remained registered? What would cause the difference, and how much would it be?

#### IV. Paperwork Reduction Act

The proposed form amendment and certain provisions of the proposed rule contain "collection of information" requirements within the meaning of the Paperwork Reduction Act of 1995 (44 U.S.C. 3501 to 3520), and the Commission has submitted the amendment and proposed rule to the Office of Management and Budget ("OMB") in accordance with 44 U.S.C. 3507(d) and 5 CFR 1320.11. The title for the collections of information are "Rule 202(a)(11)-2" and "Form ADV" both under the Advisers Act. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid control number.

##### *Rule 202(a)(11)-2*

Certain thrift institutions relying on the proposed rule would be deemed not to be "investment advisers" as defined in the Advisers Act. These thrifts would not be subject to any provision of the Advisers Act, including the various registration, disclosure and recordkeeping requirements under the Act. These thrifts could continue to render investment advice to customer accounts created and maintained for a fiduciary purpose if the advice is provided solely in the thrift's capacity as trustee, executor, administrator, or guardian for that account. For these thrift institutions, the proposed rule would serve to eliminate altogether the annual reporting and recordkeeping burden under the Advisers Act. As previously discussed, we estimate that approximately 34 advisers currently registered with us appear to be thrift institutions, but most engage in trust activities that would not be covered by the proposed exception.<sup>98</sup> Each thrift institution would need to assess both its current and planned trust department business in order to determine whether it would seek to rely on the proposed rule to be excluded from the Advisers Act and thus from the Act's reporting and recordkeeping requirements. Because the number of thrifts that

would qualify for the proposed exception will depend on the future business decisions of individual thrift institutions, it would be speculative to quantify the number of thrifts whose paperwork burden will be entirely eliminated as a result of the proposed rule.<sup>99</sup> Comment is requested on the number of thrift institutions that would qualify to use the proposed exception from the Advisers Act, and on the number of those qualifying thrifts that would elect to use it.

Thrifts that would be required to maintain their registration under the Advisers Act and that elected to rely on the rule with respect to certain customer accounts would be required to confirm, in an undertaking in their Form ADV (Schedule D), that they will make all trust department records available to Commission examiners, upon request. This collection of information is necessary to obtain the benefit of the proposed rule with regard to these certain accounts. The Commission staff will use this collection of information in its examination and oversight program.

The Commission estimates that compliance with the requirement to type in this brief undertaking in Form ADV would impose a total annual burden of 5 minutes for each thrift registered under the Act and relying on the rule to exclude, from the Act, its services to certain customer accounts. In addition, data contained on Thrift Financial Reports submitted by all savings associations indicate that approximately 117 savings associations have been granted trust powers.<sup>100</sup> Based on these data, the Commission estimates that approximately 117 thrift institutions could potentially take advantage of the proposed rule to exclude, from the scope of the Advisers Act, their advisory services to certain customer accounts. Accordingly, the total burden hours imposed by proposed rule 202(a)(11)-2 is estimated to be 9.75 hours annually.<sup>101</sup> The Commission believes this undertaking will not impose a significant additional recordkeeping burden on thrift institutions. The undertaking does not

<sup>99</sup> For example, some thrifts may choose to maintain their exempt activities within the thrift itself, but to move their non-exempt advisory business to another affiliate within their financial service firm complex.

<sup>100</sup> See *supra* note 70.

<sup>101</sup> 5 minutes × 117 thrifts = 585 minutes = 9.75 hours. Because the proposed rule may exempt some thrifts entirely from the definition of "investment adviser" (and thus from the paperwork burden of the Advisers Act), although all approximately 117 thrift institutions that have been granted trust powers could potentially take advantage of the proposed rule, it is possible that fewer than 117 would actually remain subject to the Advisers Act.

require that new or additional records be kept, only that existing records required under adviser or thrift regulations be made available.<sup>102</sup>

##### *Form ADV*

Thrifts that would be required to maintain their registration under the Advisers Act would also be required to check a box on their Form ADV that they are actively engaged in business as a thrift institution. This collection of information is mandatory. The Commission staff will use this collection of information in its examination and oversight program. The Commission estimates that compliance with this requirement to check a box on Form ADV would impose a total annual burden of 2 minutes per thrift responding to the question. As discussed above, the Commission estimates that as many as approximately 117 thrift institutions may be required to register with us and respond to this question. Accordingly, the total annual burden imposed by this collection of information is estimated to be 3.9 hours.<sup>103</sup>

Any information received by the Commission related to the proposed rule and form amendment would not be kept confidential. Pursuant to 44 U.S.C. 3506(c)(2)(B), the Commission solicits comments (i) to evaluate whether the proposed collections of information are necessary for the proper performance of the functions of the agency, including whether the information will have practical utility; (ii) to evaluate the accuracy of the agency's estimate of the burden of the proposed collections of information; (iii) to enhance the quality, utility, and clarity of the information to be collected; and (iv) to minimize the burden of these collections of information on those who are to respond, including through the use of automated collection techniques or other forms of information technology.

Persons desiring to submit comments on these collection of information requirements should direct them to the Office of Management and Budget, Attention: Desk Officer for the Securities and Exchange Commission, Office of Information and Regulatory Affairs, Washington, D.C. 20503, and also should send a copy of their comments to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Stop 6-9, Washington, DC 20549 with

<sup>102</sup> The OTS requires that records be maintained for fiduciary accounts. See 12 CFR 550.410 (requiring thrifts overseen by the OTS to keep adequate records for all fiduciary accounts).

<sup>103</sup> 2 minutes × 117 thrifts = 234 minutes = 3.9 hours.

<sup>98</sup> See *supra* note 84.

reference to File No. S7-20-04. OMB is required to make a decision concerning the collection of information requirements between 30 and 60 days after publication. A comment to OMB is best assured of having its full effect if OMB receives it within 30 days of publication.

#### V. Regulatory Flexibility Act

Pursuant to section 605(b) of the Regulatory Flexibility Act,<sup>104</sup> the Commission hereby certifies that proposed rule 202(a)(11)-2, proposed rule 12g-6, and the proposed amendment to Form ADV would not, if adopted, have a significant economic impact on a substantial number of small entities. Proposed rule 202(a)(11)-2 and the proposed amendment would except savings associations from the Advisers Act when they provide investment advice as part of certain trust department fiduciary services and revise the investment adviser registration form so that registrants could identify themselves as savings associations. Based on data reported by all savings associations in their September 30, 2003 Thrift Financial Reports (TFRs), there are no thrifts that meet the definition of a "small business" for purposes of the Advisers Act.<sup>105</sup> Proposed rule 12g-6 would exempt collective trust funds maintained by savings associations from the registration and reporting requirements of the Exchange Act. Based on the same TFR data, there are no thrift-managed collective trust funds that meet the definition of a "small business issuer" for purposes of the Exchange Act.<sup>106</sup> No other entities would incur obligations from or otherwise be directly affected by the proposed rules and amendment. Accordingly, the Commission certifies that proposed rule 202(a)(11)-2, proposed rule 12g-6, and the proposed amendment to Form ADV would not have a significant economic impact on a substantial number of small entities.

<sup>104</sup> 5 U.S.C. 605(b).

<sup>105</sup> Under Commission rules, for the purposes of the Advisers Act and the Regulatory Flexibility Act, an investment adviser generally is a small entity if it: (i) Has assets under management having a total value of less than \$25 million; (ii) did not have total assets of \$5 million or more on the last day of its most recent fiscal year; and (iii) does not control, is not controlled by, and is not under common control with another investment adviser that has assets under management of \$25 million or more, or any person (other than a natural person) that had \$5 million or more on the last day of its most recent fiscal year. 17 CFR 275.0-7(a).

<sup>106</sup> Under Commission rules, for the purposes of the Exchange Act and the Regulatory Flexibility Act, an issuer is generally is a small entity if it did not have total assets of \$10 million or more on the last day of its most recent fiscal year. 17 CFR 240.0-10(a).

The Commission requests written comments regarding this certification. The Commission requests that commenters describe the nature of any impact on small businesses and provide empirical data to support the extent of the impact.

#### VI. Statutory Authority

We are proposing rule 202(a)(11)-2 pursuant to our authority under sections 202(a)(11)(F) and 211(a) of the Advisers Act.<sup>107</sup> Section 202(a)(11)(F) gives us authority to except, by rule or order, from the statutory definition of "investment adviser" persons not within the intent of that definition. Section 211(a) gives us authority to classify, by rule, persons and matters within our jurisdiction and to prescribe different requirements for different classes of persons, as necessary or appropriate to the exercise of our authority under the Act.

We are proposing amendments to Form ADV under section 19(a) of the Securities Act of 1933,<sup>108</sup> sections 23(a) and 28(e)(2) of the Securities Exchange Act of 1934,<sup>109</sup> section 319(a) of the Trust Indenture Act of 1939,<sup>110</sup> section 38(a) of the Investment Company Act of 1940,<sup>111</sup> and sections 203(c)(1), 204, and 211(a) of the Investment Advisers Act of 1940.<sup>112</sup>

We are proposing rule 12g-6 pursuant to our authority under section 12(h) of the Exchange Act.<sup>113</sup> Section 12(h) gives us authority to, by rules or regulations, exempt any issuer or class of issuers from the provisions of section (g) of the Exchange Act, if we find by reason of the nature and extent of the activities of the issuer that such action is not inconsistent with the public interest or the protection of investors. Section 12(h) also gives us authority to classify issuers and prescribe requirements appropriate for each such class.

#### Text of Proposed Rules and Form Amendments

##### List of Subjects

##### 17 CFR Part 240

Reporting and recordkeeping requirements, Securities.

##### 17 CFR Part 275 and 279

Investment advisers, Reporting and recordkeeping requirements.

<sup>107</sup> 15 U.S.C. 80b-2(a)(11)(F) and 15 U.S.C. 80b-11(a).

<sup>108</sup> 15 U.S.C. 77s(a).

<sup>109</sup> 15 U.S.C. 78w(a) and 78bb(e)(2).

<sup>110</sup> 15 U.S.C. 77sss(a).

<sup>111</sup> 15 U.S.C. 78a-37(a).

<sup>112</sup> 15 U.S.C. 80b-3(c)(1), 80b-4, and 80b-11(a).

<sup>113</sup> 15 U.S.C. 78l(h).

For the reasons set out in the preamble, Title 17, Chapter II of the Code of Federal Regulations is proposed to be amended as follows:

#### PART 240—GENERAL RULES AND REGULATIONS, SECURITIES EXCHANGE ACT OF 1934

1. The general authority citation for Part 240 continues to read as follows:

**Authority:** 15 U.S.C. 77c, 77d, 77g, 77j, 77s, 77z-2, 77z-3, 77eee, 77ggg, 77nnn, 77sss, 77ttt, 78c, 78d, 78e, 78f, 78g, 78i, 78j, 78j-1, 78k, 78k-1, 78l, 78m, 78n, 78o, 78p, 78q, 78s, 78u-5, 78w, 78x, 78ll, 78mm, 79q, 79t, 80a-20, 80a-23, 80a-29, 80a-37, 80b-3, 80b-4, 80b-11, and 7201 *et seq.*; and 18 U.S.C. 1350, unless otherwise noted.

\* \* \* \* \*

2. Section 240.12g-6 is added to read as follows:

##### § 240.12g-6 Exemption from Section 12(g) for collective trust funds.

An issuer that is a collective trust fund excluded from the definition of an investment company under section 3(c)(1) of the Investment Company Act of 1940 shall be exempt from the requirement to register any class of equity securities pursuant to section 12(g)(1) of the Act (15 U.S.C. 78l(g)(1)).

#### PART 275—RULES AND REGULATIONS, INVESTMENT ADVISERS ACT OF 1940

3. The general authority citation for Part 275 continues to read as follows:

**Authority:** 15 U.S.C. 80b-2(a)(11)(F), 80b-2(a)(17), 80b-3, 80b-4, 80b-4a, 80b-6(4), 80b-6a, 80b-11, unless otherwise noted.

\* \* \* \* \*

4. Section 275.202(a)(11)-2 is added to read as follows:

##### § 275.202(a)(11)-2 Certain thrift institutions deemed not to be investment advisers.

(a) A thrift institution will be deemed not to be an investment adviser if the thrift institution limits its investment advisory services to the following:

(1) Investment advisory services that the thrift institution performs solely in its capacity as trustee, executor, administrator, or guardian for trusts, estates, guardianships and other accounts created and maintained for a fiduciary purpose, provided that the thrift institution does not, except in connection with the ordinary advertising of its services as trustee, executor, administrator, or guardian for such accounts, hold itself out generally to the public as providing investment advisory services.

(2) Investment advisory services for a collective trust fund maintained by the

thrift institution and excluded from the definition of the term "investment company" under section 3(c)(11) of the Investment Company Act of 1940, and for accounts the assets of which are invested solely in one or more such collective trust funds.

**Note to paragraph (a)(1):** Under paragraph (a)(1), each account to which the thrift institution provides investment advisory services must be created and maintained for a fiduciary purpose, whether that account is a trust, an estate, a guardianship or another type of account.

(b) A thrift institution will not be deemed to be an investment adviser with respect to accounts for which it provides investment advisory services that do not subject the thrift institution to the Act, but only if the thrift institution confirms in an undertaking on Schedule D of its Form ADV (17 CFR 279.1) that it will make available to Commission examiners, upon request, all trust department records. Such records shall be considered examination records under section 210(b) of the Act (15 U.S.C. 80b-10(b)).

(c) The term *thrift institution* means a "savings association" as that term is defined in sections 3(b)(1) and of the Federal Deposit Insurance Act (12 U.S.C. 1813(b)(1)) that has deposits insured by the Federal Deposit Insurance Corporation under the Federal Deposit Insurance Act (12 U.S.C. 1811), and that is not operated for the purpose of evading the provisions of the Investment Advisers Act of 1940.

**PART 279—FORMS PRESCRIBED UNDER THE INVESTMENT ADVISERS ACT OF 1940**

5. The authority citation for Part 279 continues to read as follows:

**Authority:** The Investment Advisers Act of 1940, 15 U.S.C. 80b-1, *et seq.*

6. Item 6A of Part 1A of Form ADV (§ 279.1) is amended to read as follows:  
Form ADV

*	*	*	*	*
Part 1A				
*	*	*	*	*
Item 6 Other Business Activities				
*	*	*	*	*

A. You are actively engaged in business as a (check all that apply):

- (1) Broker-dealer
- (2) Registered representative of a broker-dealer
- (3) Futures commission merchant, commodity pool operator, or commodity trading advisor
- (4) Real estate broker, dealer, or agent
- (5) Insurance broker or agent
- (6) Bank (including a separately identifiable department or division of a bank) or thrift institution
- (7) Other financial product salesperson (specify):

**Note:** The text of Form ADV does not and the amendment will not appear in the Code of Federal Regulations.

\* \* \* \* \*

Dated: April 30, 2004.  
By the Commission.

**Jill M. Peterson,**

*Assistant Secretary.*

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