FINANCIAL SERVICES INSTITUTE
VOICE OF INDEPENDENT BROKER-DEALERS AND INDEPENDENT FINANCIAL ADVISORS
www.financialservices.org

VIA ELECTRONIC MAIL

May 16, 2008

Nancy M. Morris
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

RE: File Number S7-10-00 – Form ADV Part 2

Dear Ms. Morris:

On March 3, 2008, the Securities and Exchange Commission (SEC) published proposed amendments to Part 2 of Form ADV (Proposed Amendment).[1] Form ADV Part 2 is used by investment advisers to satisfy the written disclosure statement requirement of SEC Rule 204-3. The Proposed Amendment is meant to complete the SEC's overhaul of Form ADV that began in 2000.[2] The purpose of the Proposed Amendment is to require investment advisers to provide clients and prospective clients with a clear, current, and meaningful disclosure of the business practices, conflicts of interest, and background of the investment adviser and its advisory personnel. The Proposed Amendment would replace the current "check-the-box" format of Form ADV Part 2 and related disclosure schedules with a plain English, narrative brochure. The brochure would contain enhanced disclosure of potential conflicts of interest and would incorporate the disclosure of legal and disciplinary events involving the investment adviser firm and its management personnel.

The Financial Services Institute[3] (FSI) appreciates this opportunity to comment on the Proposed Amendment. While FSI strongly supports the SEC's efforts to amend Form ADV Part 2 and make it available via the Internet, we believe certain improvements to the Proposed Amendment must be made to improve the effectiveness of the disclosures, provide the industry with necessary regulatory clarity, and reduce the cost of compliance.

Background on FSI Members

The Independent Broker-Dealer (IBD) community has been an important and active part of the lives of American consumers for more than 30 years. The IBD business model focuses on comprehensive financial planning services and unbiased investment advice. IBD members also share a number of other similar business characteristics. They generally clear their securities business on a fully disclosed basis; primarily engage in the sale of packaged products, such as mutual funds and variable insurance products, by "check and application"; take a comprehensive approach to their clients' financial goals and objectives; and provide investment advisory services through either affiliated registered investment advisor firms or such firms owned by their registered representatives. Due to their unique business model, IBDs and their affiliated financial

[1] See Inv. Advisers Act Rel. No. 2711 (March 4, 2008) at http://sec.gov/rules/proposed/2008/ia-2711fr.pdf.
[2] See Inv. Advisers Act Rel. No. 1862 (April 5, 2000) at http://sec.gov/rules/proposed/34-42620.htm.
[3] The Financial Services Institute, Voice of Independent Broker-Dealers and Independent Financial Advisors, was formed on January 1, 2004. Our members are broker-dealers, often dually registered as federal investment advisers, and their independent contractor registered representatives. FSI has 119 Broker-Dealer member firms that have more than 138,000 affiliated registered representatives serving more than 14 million American households. FSI also has more than 12,500 Financial Advisor members.

advisors are especially well positioned to provide middle class Americans with the financial advice, products, and services necessary to achieve their financial goals and objectives.

In the U.S., approximately 98,000 independent financial advisors – or approximately 42.3% percent of all practicing registered representatives – operate in the IBD channel.[4] These financial advisors are self-employed independent contractors, rather than employees of the IBD firms. These financial advisors provide comprehensive and affordable financial services that help millions of individuals, families, small businesses, associations, organizations, and retirement plans with financial education, planning, implementation, and investment monitoring. Clients of independent financial advisors are typically "main street America" – it is, in fact, almost part of the "charter" of the independent channel. The core market of advisors affiliated with IBDs is clients who have tens and hundreds of thousands as opposed to millions of dollars to invest. Independent financial advisors are entrepreneurial business owners who typically have strong ties, visibility, and individual name recognition within their communities and client base. Most of their new clients come through referrals from existing clients or other centers of influence.[5] Independent financial advisors get to know their clients personally and provide them investment advice in face-to-face meetings. Due to their close ties to the communities in which they operate their small businesses, we believe these financial advisors have a strong incentive to make the achievement of their clients' investment objectives their primary goal.

FSI is the advocacy organization for IBDs and independent financial advisors. Member firms formed FSI to improve their compliance efforts and promote the IBD business model. FSI is committed to preserving the valuable role that IBDs and independent advisors play in helping Americans plan for and achieve their financial goals. FSI's primary goal is to insure our members operate in a regulatory environment that is fair and balanced. FSI's advocacy efforts on behalf of our members include industry surveys, research, and outreach to legislators, regulators, and policymakers. FSI also provides our members with an appropriate forum to share best practices in an effort to improve their compliance, operations, and marketing efforts.

The Proposed Amendment is of particular interest to FSI. We support the SEC's objective of providing clients with "sufficient information about the adviser and its personnel to permit them to make an informed decision about whether to engage an adviser, and having engaged the adviser, how to manage the relationship."[6] However, we believe that certain improvements to the Proposed Amendment would improve the effectiveness of the disclosures, provide the industry with necessary regulatory clarity, and reduce the cost of compliance. Our specific comments are discussed below.

<u>Comments on the Proposed Amendment</u>
FSI offers the following comments on the Proposed Amendment:

- Improve Effectiveness of Disclosure Through Focus Group Testing – While we understand and appreciate the SEC's goal of providing clients with current and meaningful disclosure, the Proposed Amendment seems at odds with the findings of the RAND Study[7] and the SEC's

[4] Cerulli Associates Quantitative Update: Advisor Metrics 2007, Exhibit 2.04. Please note that this figure represents a subset of independent contractor financial advisors. In fact, more than 138,000 financial advisors are affiliated with FSI member firms. Cerulli Associates categorizes the majority of these additional advisors as part of the bank or insurance channel.
[5] These "centers of influence" may include lawyers, accountants, human resources managers, or other trusted advisors.
[6] See Inv. Advisers Act Rel. No. 2711 (March 4, 2008) at http://sec.gov/rules/proposed/2008/ia-2711fr.pdf.
[7] See the RAND Study at http://www.sec.gov/news/press/2008/2008-1_randiabdreport.pdf.

recent Summary Prospectus proposal.[8] The results of the RAND Study clearly indicate that detailed disclosure documents do not aid retail clients in their understanding of their investments and advisory relationships.[9] In its Summary Prospectus proposal, the SEC itself acknowledges that consumers of investment products want short, concise disclosure documents.[10] Unfortunately, the Proposed Amendment does not put these lessons into practice. Instead, it creates a long and detailed disclosure document that will likely go unread by many advisory clients who will be intimidated by its bulk. We recommend that the draft Brochure, and related disclosures, be presented to focus groups made up of retail investors to test their effectiveness. Focus groups could also identify the information investors believe is "material" for purposes of clarifying the SEC's definition of this term. We believe these efforts will reveal substantial opportunities to improve the Proposed Amendment and create a more effective disclosure document. This approach would have the ancillary benefit of delaying the Proposed Amendment until the SEC's review of the RAND Study is complete. Such a delay would insure coordination of the Proposed Amendment with that initiative to the benefit of advisory clients and the industry.

- Modify Requirement for Annual Mailing of Part 2 – The SEC indicates that delivering an updated Form ADV Part 2A ("Brochure") annually to clients will create an annual burden of 253.25 hours per advisor. IBD firms report that these estimates vastly underestimate the burden associated with the mailing requirement. In addition, most investment advisers report that clients do not want and will not read an annual updated Brochure. In fact, one FSI member firm reports that despite offering to deliver the current Form ADV Part 2 to some 700,000 clients annually, they have received fewer than 10 requests for the document during the past several years. This experience leads us to conclude that clients simply are not interested in receiving the annual updates of the Brochure. It is, therefore, difficult to justify the significant expense of coordinating the timely creation, printing, and delivery of the updated Brochure to advisory clients. As a result, we suggest that advisers be required annually to inform their clients of their right to obtain a Brochure and any amendments electronically through the IARD system or by contacting the adviser. We believe this approach is consistent with recent SEC rulemaking proposals that have adopted an "access equals delivery" disclosure model.[11] However, if the SEC insists upon an annual mailing, we suggest that the mailing consist of a summary of material changes to the adviser's Brochure together with information on how clients may obtain a hard copy Brochure via the IARD or by contacting the adviser.

- Eliminate Requirement for Interim Delivery of Brochure – The Proposed Amendment would also require the delivery of an updated Brochure if the disclosure is amended to add or materially change disciplinary event information or if other information becomes materially inaccurate. Unfortunately, materiality remains a subjective principal under the Proposed Amendment.[12] As a result of this lack of clarity, advisers are likely to exercise an abundance of caution in determining when the delivery of an interim update is required. We fear the result

[8] See the Summary Prospectus Proposal entitled "Enhanced Disclosure and New Prospectus Delivery Option for Registered Open-End Management Investment Companies" Release Nos. 33-8861 and IC-28064 (November 1, 2007) at http://sec.gov/rules/proposed/2007/33-8861fr.pdf.
[9] See page xxii of the Executive Summary to the RAND Study.
[10] See Summary Prospectus Proposal at 72 Fed Reg. 67791.
[11] See "Enhanced Disclosure and New Prospectus Delivery Option for Registered Open-End Management Investment Companies", Release No. 40-28064 (Nov. 21, 2007), "Securities Offering Reform", Rel. Nos. 33-8591, 34-52056, and IC-26993 (July 19, 2005), "Shareholder Choice Regarding Proxy Materials", Rel. Nos. 34-56135 and IC-27911 (July 26, 2007), and "Enhanced Disclosure and New Prospectus Delivery Option for Registered Open-End Management Investment Companies" Release Nos. 33-8861 and IC-28064 (November 1, 2007).
[12] As mentioned above, FSI recommends that the SEC utilize focus group testing to learn the specific information investors deem to be "material" for purposes of clarifying the definition of this term.

will be frequent interim disclosure of information of minimal relevance to clients. Such a practice will have the unfortunate consequence of undermining the effective disclosure of information relevant to advisory clients. As a result, we recommend that the SEC eliminate the interim delivery requirement in favor of an annual requirement to inform clients of their right and ability to obtain a Brochure and any amendments electronically through the IARD system or by contacting the adviser.

- Modify Summary of Brochure Changes Requirement – Item 2 of Part 2A would require advisers to prepare a summary of material changes to the Brochure since the last annual update. The summary would appear on the cover page of the Brochure or immediately thereafter, or could be included in a separate communication that would accompany the Brochure. Absent a clear definition of the term "material changes", FSI is concerned that advisers may be tempted to provide a summary of all year-over-year changes to their Brochure in an effort to mitigate regulatory and liability exposure resulting from after-the-fact determinations of materiality. We believe such an approach would frustrate the SEC's goal of providing a concise summary of changes to the Brochure. As a result, we again encourage the SEC to consult focus groups to identify the information investors find "material" to their choice of investment advisor. This information should be used to provide a specific definition of material changes. In the alternative, we recommend that the SEC simply change Item 2 to require a summary of year-over-year changes without the necessity of determining their materiality.

- Modify the Fees and Compensation Disclosure – Item 5 of Part 2A would require the Brochure to include a description of how the adviser is compensated for providing advisory services and to describe the types of other expenses , such as brokerage, custody fees, and fund expenses, that clients may pay in connection with the advisory services provided to them by the adviser. In addition, Item 5.E. would require advisers that receive brokerage commissions for the sale of a security or other investment product to disclose this practice, the conflict of interest it creates, and how the adviser addresses this conflict. We strongly disagree with the conclusion imbedded in this disclosure requirement. Many advisers with broker-dealer affiliations utilize a fee and commission compensation structure that recognizes that investment advisory services are distinct from transaction execution services. Instead of endorsing one compensation structure over another, we urge the SEC to revise the disclosure so that it is designed to provide clients with a clear understanding of the way in which their adviser may be compensated.

- Define "Frequent Trading" – Item 8 of Part 2A would require the Brochure to include specific disclosures if an adviser engages in "frequent trading." However, the Proposed Amendment fails to define the term, stating that the lack of definition will provide advisers flexibility. While we appreciate the difficulty inherent in defining the term "frequent trading" and the SEC's desire to provide firms with flexibility, advisers seek the regulatory certainty needed to prepare the Brochure with confidence. As a result, we urge the SEC to either develop a definition for the term or eliminate the specific disclosure requirement. After all, if the SEC itself cannot define the term "frequent trading" then it is manifestly unfair to sanction firms whose definition is later determined to fall short.

- Provide a More Descriptive Name for Part 2B – The SEC has chosen the term "Brochure Supplement" to refer to Part 2B (Brochure Supplement). This term should be replaced with a more descriptive term that explains the purpose of the document. A more descriptive title would alleviate confusion for both the client and for industry professionals. FSI suggests the term "Investment Adviser Representative Fact Sheet" be adopted as the name of the Part 2B.

- Define "Substantial" Income and Time – Item 4 of the Part 2B would require a supervised person who engages in non-investment-related business activities that provide a substantial source of their income or that involve a substantial amount of their time to disclose this information in their Brochure Supplement. The SEC, however, does not define the term "substantial." The SEC states that they prefer instead to leave some flexibility for advisers to determine if the activity is a substantial source of income or substantial demand on the supervised person's time. We believe the SEC should define the terms "substantial source of income" and "substantial amount of time" by establishing uniform definable percentages for each. We believe this approach will provide advisers with the regulatory certainty they need to prepare the Supplement with confidence.

- Eliminate Brochure Supplement Disclosures Concerning Supervision – The Proposed Amendment would require the Brochure Supplement to include an explanation of how the firm monitors the advice provided by the supervised person. The investment adviser would also have to provide the client with the name, title and telephone number of the person responsible for supervising the advisory activities of the supervised person. While we understand the SEC's desire to provide advisory clients with a means to contact other advisory personnel when necessary to address problems in the advisory relationship, we believe the proposed method is problematic. It is common in the IBD channel for advisory personnel to be supervised by multiple persons. For example, certain individuals may supervise the nature and quality of their investment advice, while others supervise their advertising materials, and still other persons might supervise other activities. These supervisors may be operating from more than one location. As a result, tracking the impact of employee turnover or changes in job responsibilities on the Brochure Supplement will become a difficult and time consuming task within large independent investment adviser firms. Therefore, we encourage the SEC to eliminate the supervision disclosures from the Brochure Supplement. Instead, the Proposed Amendment should require the firm to list in the Brochure Supplement a toll free number and/or e-mail address that can be used by clients to contact the adviser with their concerns or questions.

- Mandate Use of FINRA's BrokerCheck System for Brochure Supplements – FSI believes the Proposed Amendment would be improved by creating a centralized database for Brochure Supplement information. Dual registrants have already supplied the required information to FINRA through the filing and periodic maintenance of their Form U-4. FINRA currently administers both the IARD and BrokerCheck systems. We encourage the SEC to take advantage of these data depositories and delivery mechanisms by mandating the filing of Brochure Supplement information on Form U-4 via an expanded CRD system designed to accommodate investment adviser representatives. Such a database could be used by advisory clients to gain information about their investment adviser representative and other relevant personnel. In addition, the Brochure Supplement depository would provide regulators the advantage of a shared database of investment adviser representative information. Finally, the Brochure Supplement depository would eliminate the burden of duplicate filings in different systems and, thereby, eliminate the possibility of inconsistent or conflicting disclosures.

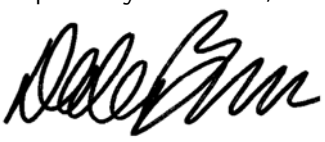
- Do Not Require the Use of XBRL – The Proposed Amendment seeks comments about whether advisers should be required to file brochure information using XBRL. XBRL is a language for electronic communications of business and financial data that allows for the tagging of data to facilitate the preparation, publication, and analysis of that information by software applications. We oppose the SEC mandating the use of XBRL because we believe this requirement would be too costly for smaller investment advisory firms and of limited benefit to their clients.

Conclusion

We are committed to constructive engagement in the regulatory process and, therefore, would welcome the opportunity to work with you to develop a disclosure regime that will provide advisory clients and prospective clients sufficient information to make informed decisions about those offering advisory services.

Thank you for your consideration of our comments. Should you have any questions, please contact me at 770 980-8487.

Respectfully submitted,



Dale E. Brown, CAE
President & CEO