

CONSULTANT PUBLICATIONS INCORPORATED

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SEC LETTER

December 30, 1974
Mr. Barry Allen Reiss
705 Mayer Central Building
3033 North Central Avenue
Phoenix, AZ 85012

Dear Mr. Reiss:

Your letter of November 8, 1974 to Miles V. Gordon of the Commission's Los Angeles Regional Office has been forwarded to us for our comment. This office has administrative responsibility within the Commission for interpretation of the Investment Advisers Act of 1940 ('Advisers Act'). You have asked about our interpretation of Section 206 of the Advisers Act with respect to the size of investment advisory fees and with respect to refunds upon cancellation of advisory contracts.

With respect to the size of investment advisory fees, it is our position that an annual investment advisory fee of more than 2% of assets under management is higher than that normally charged by persons in the investment advisory industry and that any investment adviser who charges more than 2% would be violating the antifraud provisions of Section 206 unless he discloses to existing and potential clients that his fee is higher than that normally charged in the industry and that other investment advisers provide the same or similar services at lower rates. The disclosure may also include an explanation, if appropriate, of how the particular services differ from those generally provided by other advisers. An investment adviser is a fiduciary who is or has a duty of undivided loyalty to his clients. One such duty would be the duty to disclose his fee structure in a meaningful way to his clients, including the fact his fee exceeds the 2% established norm; of course, he can also use that opportunity to explain why his fees are higher.

With respect to refunds of advisory fees paid upon cancellation of advisory contracts, Section 205(2) of the Advisers Act states that advisory contracts must provide in substance that the advisory contract cannot be assigned without the consent of the advisee. We would interpret the antifraud provisions of Section 206 to apply to any advisory contract which, upon cancellation or termination, did not provide in substance for a pro rata refund of a prepaid investment advisory fee. To take any other positions would render essentially meaningless the protection for investors, provided by Congress in Section 205(2). See Section 208(d) of the Act. Accordingly, any advisory contract which does not provide in substance for a pro rata refund of a prepaid investment advisory fee would raise serious questions and could, in our opinion, violate the antifraud provisions of Section 206 of the Advisory Act.

We trust this responds to the questions you have raised.

Sincerely,

Alan Rosenblat
Chief Counsel
by: Martin E. Lybecker
Attorney

INCOMING LETTER

November 8, 1974
Securities and Exchange Commission
Regional Office
312 North Spring Street
Los Angeles, California 90012
Attention: Miles V. Gordon

Dear Mr. Gordon:

This office represents The Consultant Publications, Inc., an Arizona corporation. Your letter of October 7, 1974, and Mr. Hasson's response of October 22, 1974, has been referred to me for reply.

Your letter indicates that your staff is of the opinion that investment advisory fees exceeding 2% of the client's assets 'may be' a violation of Sec. 206 of the Investment Advisers Act of 1940 unless proper disclosure is made. I find your conclusion both confusing and unfounded as a matter of law. Sec. 206 has not been interpreted along the lines you suggest, nor am I aware of any regulation which defines the 2% advisory fee as being excessive or illegal. If there are statutes and regulations of which I am not aware, I would appreciate your calling them to my attention.

You have also requested that The Consultant change its position regarding cancellation and refund privileges. Since your reasons are not indicated in your letter, and since Mr. Hasson has been unable to enlighten me as to your conversation, I find that I am not able to properly respond. I am personally aware of no statute or regulation which requires an investment advisory service to refund monies to subscribers if it goes out of business. If there is any such statute or regulation I would very much appreciate your calling it to my attention.

If at all possible, would you please forward to me at your very earliest convenience a copy of the up-to-date rules and regulations of the S.E.C. with respect to investment advisers and the Investment Advisers Act of 1940.

Very truly yours,

Barry Allen Reiss