AICPA® Personal Financial Planning Section

The CPA's Guide to

Investment Advisory Business Models

Have You Crossed the Line When Providing Investment Advice?

Dinsmore & Shohl LLP

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Introduction

CPAs who are providing personal financial services (including tax, estate, retirement, investment, or risk management planning) to their clients are in an optimal position to add investment advisory services to their business. Surveys show that CPAs are ranked among the most trusted advisers. They put their clients' interest first when providing advice, which is an especially critical element that the American public seeks in investment advisers. There is significant untapped revenue in the investment advisory market, but many CPAs do not enter into this line of business because they believe the regulatory issues are too complex to navigate.

The business model you select for your firm for providing investment services will determine the legal and regulatory issues you will face. The most common regulatory business models used by CPAs in providing investment services to clients are:

- *Investment Adviser*. An investment adviser (RIA or IA) provides advice to clients about investing in securities for a fee rather than a commission. This business model may require the CPA or CPA firm to register as an investment adviser with the Securities and Exchange Commission (SEC) or one or more states.
- *Investment Adviser Representative*. An investment adviser representative (IAR) provides investment advice to clients on behalf of a registered investment advisory (RIA) firm. This model may require the IAR to register with one or more states and subject the IAR to the regulatory requirements applicable to registered investment advisers.
- *Solicitor*. A solicitor "finds" and refers clients to a financial services professional for a fee. A solicitor may be required to register as an IA or IAR in some states.
- *Registered Representative*. A registered representative (RR) is licensed to sell securities for a broker-dealer and receives a commission on the sale. An RR is required to register with the Financial Industry Regulatory Authority (FINRA) and is subject to the regulatory requirements applicable to FINRA member broker-dealers.

The threshold question you must consider is whether the type and frequency of your financial advisory services to clients will subject you to regulation. Federal and state securities laws define an "investment adviser" as a person or entity who, for compensation, is engaged in the business of providing advice on securities. Federal and state securities regulators interpret this definition broadly. For example, you may be providing investment advice if, among other services, you:

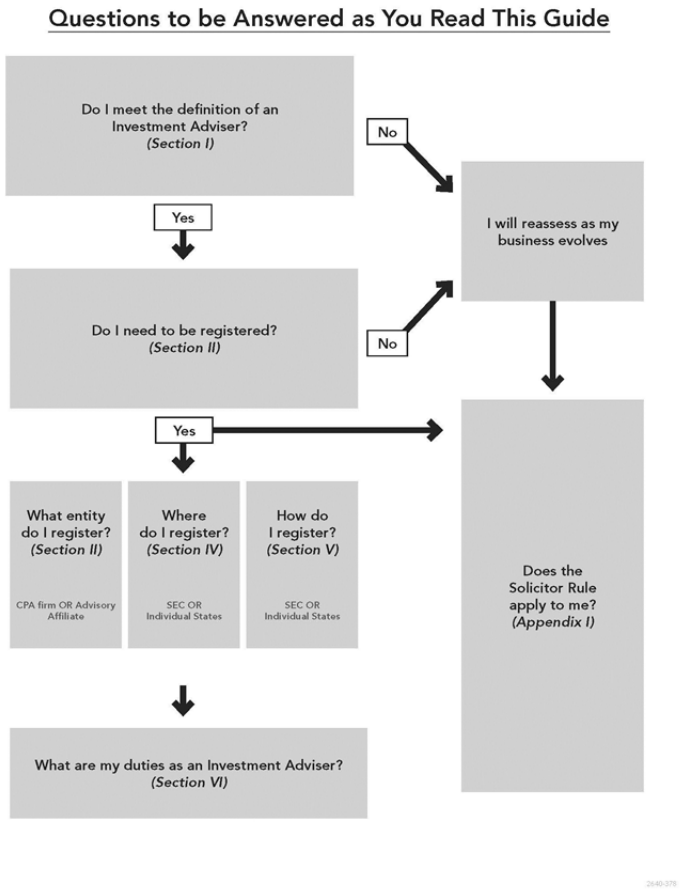
- Recommend asset allocation;
- Provide advice as to the selection or retention of an investment manager;
- Provide advice concerning securities even if not related to specific securities;
- Are in the business of providing investment advice; or
- Receive compensation for any of the above services.

If you meet this definition in connection with your PFP activities, you will be subject to federal and state investment adviser registration and regulation unless an exclusion or exemption is available.

The most common regulatory business model for CPAs providing PFP services is the investment adviser model. This Guide is intended to assist AICPA members in understanding the registration and regulatory provisions applicable to investment advisers under the Investment Advisers Act of 1940[1] and similar laws adopted by the various states. In this Guide, you will find information on determining when you cross the line between providing investment advice "solely incidental" to your practice and providing investment advice that is not "solely incidental," CPA standards of professional conduct implicated when providing investment advice or services, the business models available for your firm in providing personal financial services (Appendix 1), and resources available to you as you start or grow a PFP practice (Appendix 2).

The AICPA has also created a guide, *The CPA's Guide to Developing and Managing a PFP Practice*, for the CPA who wants to add PFP services as another value-added service.

Certain definitions used in this Guide are set forth in Appendix 3.



[1] Advisers Act, 15 U.S. C. §80-b.

Who Is An Investment Adviser?

Investment Adviser Defined

The Investment Advisers Act of 1940 ("Advisers Act") defines an investment adviser as:

> Any person[2] who, **for compensation**, engages **in the business of advising others**, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities[3] [emphasis added].

Whether a person (including both a natural person and a partnership, limited liability company, corporation, or other entity) is an investment adviser within the meaning of the Advisers Act depends on whether the person: (1) provides advice, or issues reports or analyses, regarding securities; (2) is in the business of providing such services; and (3) provides such services for compensation.[4] Each of these elements must be present before a person will be deemed an "investment adviser."

"ADVICE REGARDING SECURITIES"

The "advice regarding securities" standard requires that advisory services be provided with respect to an instrument that satisfies the Advisers Act's definition of a *security* and with which there is a judgmental element in connection with the advice.

What Is a Security?

Many CPAs may assume that a "security" only refers to a stock or bond that is traded on a national exchange. In fact, under federal and state securities laws, the definition of a "security" is very broad and, in addition to stocks and bonds (whether or not publicly traded) includes (i) promissory notes, (ii) limited partnership or limited liability company interests, (iii) fractional interests in oil or gas leases, (iv) interests in any profit-sharing agreement, (v) investment contracts, and (vi) a variety of other rights relating to securities.[5] The U.S. Supreme Court has

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[2] For the purposes of the Advisers Act, the term "person" refers to any natural person or any entity, such as a corporation, limited liability company, or other entity. Section 202(a)(16) of the Advisers Act, 15 U.S.C. §80b-2(a)(16).

[3] Advisers Act §202(a)(11), 15 U.S.C. §80b-2(a)(11).

[4] Applicability of the Investment Advisers Act to Financial Planners, Pensions Consultants, and Other Persons Who Provide Investment Advisory Services as a Component of Other Financial Services, Investment Advisers Act Release No. IA-1092, 39 S.E.C. Docket 494, 1987 WL 112702 (Oct. 8, 1987) (hereafter referred to as "Release No. IA-1092").

[5] See Section 2(a)(1) of the Securities Act of 1933, which provides that, "unless the context otherwise requires," the term "security" includes:

> Any note, stock, treasury stock, security future, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, any put, call, straddle, option, or privilege on any security certificate of deposit, or group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency, or, in general, any interest or instrument commonly known as a "security", or any certificate of

said that the definition of a "security" includes "the countless and variable schemes devised by those who seek the use of the money of others."[6]

Must Advice Relate to Specific Securities?

The seminal authority on the applicability of the Advisers Act to persons who provide investment advisory services as a component of other financial services is contained in Release No. IA-1092, issued by the United States Securities and Exchange Commission (SEC) in 1987. (The release is Appendix 4 to this Guide). In Release No. IA-1092, the SEC addressed the issue of whether advice, recommendations, or reports that do not pertain to *specific* securities satisfy the "advice regarding securities" element of the definition. In the release, the SEC took the position that, assuming the services are being performed as part of a business and for compensation, the SEC staff "believes that a person who provides advice, or issues or promulgates reports or analyses, **which concern securities, but which do not relate to specific securities**" *generally will fall under the definition of investment adviser.* The release also noted that the SEC staff has interpreted the definition of investment adviser to include persons who advise clients concerning the relative advantages and disadvantages of investing in securities *in general* as compared to other investments.[7] Under some circumstances, recommending an investment adviser to a client may itself trigger investment adviser registration.[8]

"IN THE BUSINESS OF"

The critical determination under the "business" element is whether the degree of the advisory activities constitutes being "in the business of" an investment adviser.[9] The SEC looks at all facts and circumstances surrounding a person's activities to determine whether a person is "in the business of" giving advice about securities for compensation. The giving of such advice need not constitute the principal business activity or any particular portion of the business activities of a person. The giving of advice need only be done on such a basis that it constitutes a business activity with some regularity. Relevant factors include, but are not limited to:

- Whether the person represents or otherwise holds himself out to the public as an investment adviser;
- Whether the person receives separate or additional compensation representing a clearly definable charge for giving advice about securities; and
- The frequency or regularity of providing "specific investment advice."[10]

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interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.

[6] *Marine Bank v. Weaver*, 455 U.S. 551, 555 (1982). See also *SEC v. W.J. Howey Co.*, 328 U.S. 293 (1946).

[7] Release No. IA-1092, *supra*, footnote 4.

[8] See, e.g., FPC Securities Corp., SEC No-Action Letter (Dec. 1, 1974) (program to assist client in selection and retention of investment manager by, among other things, recommending investment managers to clients, monitoring and evaluating the performance of a client's investment manager, and advising client as to the retention of such manager).

[9] Release No. IA-1092, *supra*, footnote 4. See also Section II of this Guide.

[10] Id.

The term "specific investment advice" includes a recommendation, analysis, or report about specific securities or specific categories of securities, or a recommendation that a client allocate certain percentages of his assets to life insurance, high-yielding bonds and mutual funds, or particular types of mutual funds.[11] The term does not include advice limited to general recommendations to allocate assets among, for example, securities, life insurance, and tangible assets.[12]

"FOR COMPENSATION"

The "for compensation" element is satisfied by the receipt of *any* economic benefit. The SEC has stated that the compensation element is satisfied if a single fee is charged for a number of different services, including investment advice or the issuing of reports or analyses concerning securities.[13] It is not necessary that the compensation be paid directly by the person receiving the investment advisory services.[14] Thus, if an adviser earns a commission from a third party for the sale of an investment product, that commission satisfies the "for compensation" element.[15]

Difference Between Investment Adviser and Financial Planner

The difference between an investment adviser and a financial planner is the services provided, though these two categories are hardly distinct and, depending on the services provided, may blend into each other. An investment adviser advises clients on investing in securities. A financial planner evaluates all aspects of a client's financial needs, including savings, investments, education, insurance, taxes, retirement, and estate planning, and then creates a financial plan tailored to the client to meet the client's financial goals. Financial plans can be provided using various tools, including questionnaires, online services, and software. Some financial planners may specialize in one or more areas or recommend a limited range of financial advice. Whether services are provided as an investment adviser or a financial planner, or advice regarding retirement or estate planning is given, if the advice concerns securities, the person would likely fall under the definition of "investment adviser" and need to register with the proper regulatory authority.

Do I Need to Register as an Investment Adviser?

If a person falls within the three-part "investment adviser" definition described in the previous section of this Guide, then generally the person would be subject to either state or SEC registration. CPAs, however, may be exempt from registration under certain limited circumstances.

[11] Id.
[12] Id.
[13] Id. (citing, e.g., FINESCO, SEC No-Action Letter [Dec. 11, 1979]).
[14] Id.
[15] Id. See also Thomas P. Lemke and Gerald T. Lins, *Regulation of Investment Advisers* §1:4 (West 2012 Edition) (hereafter cited as "Regulation of Investment Advisers").

Are CPAs Exempted from Registration as an Investment Adviser?

As a CPA, you may be excluded from the investment adviser definition if the advice you provide is "solely incidental" to the practice of your profession.[16] The Advisers Act does not define the term "solely incidental." As a result, the determination of whether this exclusion is available depends on the facts and circumstances of each situation.

ARE INVESTMENT SERVICES YOU PROVIDE "SOLELY INCIDENTAL" TO ACCOUNTING SERVICES RENDERED TO CLIENTS?

The SEC has identified three factors that are particularly relevant in determining whether investment services are "solely incidental" to accounting services:

- Whether the accountant holds himself out to the public as an investment adviser or financial planner;
- Whether the professional's fee structure for investment advisory services is different from the schedule for the professional services; and
- Whether the advice given is in connection with and reasonably related to the professional services rendered.[17]

If you satisfy any **one** of these three factors, you may lose the exemption provided to accountants.[18]

Holding Out to the Public

In several "no-action" letters[19], the SEC has taken the position that, when an accountant holds himself out publicly as providing *financial planning*, pension consulting, or other financial advisory services, the performance of those services is not *solely incidental* to his practice as an accountant.[20] In other words, the SEC's position is that every CPA who holds himself out to the public as a financial planner or pension consultant or as a provider of other financial advisory services is, by definition, an "investment adviser" who must register under the Advisers Act.[21]

The SEC has stated that a person is "holding himself out" to the public as an investment adviser if he promotes himself as providing financial planning, pension consulting, or other financial advisory services:

[16] Advisers Act §202(a)(11)(B), 15 U.S.C. §80b-2(11)(B). There are other exclusions from the definition of investment adviser; however, the discussion in this Guide has been limited to the exclusion specifically excluding accountants and the exclusion for family offices. See Section II.B. of this Guide.
[17] Regulation of Investment Advisers §1:18.
[18] See, e.g., David R. Markley, SEC No-Action Letter, 1985 WK 53850 (February 6, 1985).
[19] A "no-action" letter is a response by SEC staff to written inquiries received by the SEC, and reflects the opinion of SEC staff that, under the particular circumstances presented, staff may or may not recommend an enforcement action. No-action letters do not necessarily reflect the official position of the SEC.
[20] Release No. IA-1092, *supra*, footnote 4.
[21] See, e.g., Hungerford, Aldrin, Nichols & Carter, SEC No-Action Letter, 1991 WL 290535 (Dec. 10, 1991).

- By general advertising or general mailings;
- By using the term "financial planner" or "investment adviser" or other similar term on a business card or stationery;
- By listing himself as a financial planner or investment adviser in a telephone, business or building directory; or
- By letting it be known, through word of mouth or otherwise, that he is available to provide financial planning, investment advice, or similar advisory services.[22]

Fee Structure

For a CPA's investment services to be "solely incidental" to accounting services rendered, the CPA's fees for investment advice should be based on the same factors as the CPA uses to determine his usual charges for accounting services. The SEC has stated that investment advice would not be "solely incidental" where the accountant charges an hourly fee for accounting services and a percentage of assets fee for advisory services.[23] The SEC has also stated that even though the fees charged by an accountant for investment advice may not constitute a major or substantial part of his revenues, this factor alone does not lead to the conclusion that the person is not in the business of providing investment advice.[24]

Advice Given Is in Connection with and Reasonably Related to the Accounting Services

Of the three factors used to determine whether an accountant's investment services are "solely incidental" to accounting services rendered to a client, whether advice is given in "connection with and reasonably related to" accounting services is perhaps the least understood factor. SEC no-action letters responding to questions posed by accountants generally base the determination of whether registration as an investment adviser is required on whether the accountant is "holding himself out to the public" as an investment adviser and, to a lesser extent, on the accountant's fee structure. As a result, little guidance is available to ascertain whether investment advice is "reasonably related to" a CPA's accounting services. Nevertheless, even without more specific guidance from the SEC, if financial planning or investment advice is provided to a person who has not engaged a CPA to provide accounting services, but has instead hired the CPA *solely* for investment advice, the SEC would likely determine that registration as an investment adviser is required.

REGISTRATION OF AFFILIATED ENTITY IN LIEU OF REGISTERING ACCOUNTING FIRM

The SEC has permitted accounting firms to register an affiliated entity (as opposed to the accounting firm itself) to supervise the partners or other professionals of the accounting firm in the rendering of general investment consulting and tax planning services. To avoid the need for

[22] LaManna & Hohman, SEC No-Action Letter, 1983 WL 31009 (Mar. 21, 1983).
[23] Release No. IA-1092, *supra*, footnote 4 (citing Hauk, Sole & Fasani, P.C., SEC No-Action Letter [May 2, 1986]).
[24] George J. Dippold, SEC No-Action Letter, 1990 WL 286595 (May 7, 1990).

the accounting firm itself to register as an investment adviser, the accounting firm must satisfy the following conditions: [25]

- The accounting firm must not recommend specific securities or industry sectors (aside from tax and estate planning services);
- The advisory and personal financial planning services must be substantially similar to traditional accounting services;
- Neither the affiliated entity nor the accounting firm can have custody or possession of client funds or securities;[26]
- Personnel who participate in personal financial planning or consulting services will be deemed "advisory affiliates" and "persons associated with the investment adviser" for purposes of Form ADV and the Advisers Act;
- Amounts billed for financial planning services must be separately stated from traditional accounting services; and
- The affiliated investment adviser must keep and maintain all books and records required under the Advisers Act, including copies of any financial plans and related engagement letters, billing records and letters and other communications relating to personal financial planning clients created by the accounting firm.

Can CPAs Rely on the Family Office Exemption from Registration?

As a CPA, you may be employed or retained by an entity to provide financial management, tax planning, charitable coordination, estate planning, and other services to members of a wealthy family. The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010[27] (the "Dodd-Frank Act") added a new exclusion from the investment adviser definition for any family office as defined by SEC rules.[28]

- A "family office" is defined as an entity, including its directors, partners, managers, trustees, and employees, that meet each of the following three criteria:
  - Has only family clients;
  - Is wholly owned by family clients and exclusively controlled by one or more family members or family entities; and
  - Does not hold itself out to the public as an investment adviser.[29]

[25] See, e.g., Arthur Andersen & Co., SEC No-Action Letter, 1994 WL 381818 (July 8, 1994); Price Waterhouse, SEC No-Action Letter, 1987 WL 108420 (Oct. 1, 1987).
[26] The SEC staff may no longer consider the restriction on custody or possession of client funds or securities by the affiliated entity or the accounting firm as necessary in light of rule changes requiring registered advisers with custody of client assets to undergo an annual surprise examination by an independent public accountant. See Section VI.B of this Guide.
[27] Public Law 111-203 (July 21, 2010).
[28] Advisers Act § 202(a)(11)(G), 15 U.S.C. § 80b-2(a)(11)(G).
[29] Advisers Act Rule 202(a)(11)(G)-1, 17 C.F.R. § 275.202(a)(11)(G)-1.

"Family client" is defined to include (i) current and former family members (lineal descendants of a common ancestor) and their spouses or spousal equivalents, (ii) key employees of the family office and former key employees under certain circumstances, (iii) nonprofit organizations or charitable foundations or trusts funded exclusively by family clients, (iv) estates of family members or key employees, (v) irrevocable trusts in which family clients are the only current beneficiaries, or funded exclusively by family clients in which family clients and nonprofit or charitable organizations are the only current beneficiaries, (vi) revocable trusts of which key employees are the trustees and settlors, and (vii) companies owned exclusively by and operated for the sole benefit of family clients.

Hypothetical Examples Highlighting Registration Issues

To help CPAs apply the principles discussed in this Guide, the following examples describe circumstances under which registration as an investment adviser might be necessary. These examples are not intended as legal advice. The determination of whether registration is required depends on the specific facts and circumstances applicable in each instance, and a change in a single fact may result in a different analysis on the question of whether registration is required. No assurance can be given that the SEC or a state securities administrator might not reach a different conclusion than is suggested below.

1. Ann is a CPA who offers accounting and tax services through her accounting firm, of which she is the sole professional. On her website, Ann identifies the services she provides as "accounting and financial planning." Ann also asks Charlie and other clients to please let their friends and acquaintances know that Ann is willing to assist her accounting clients with financial planning. One of her clients, Charlie, asks Ann, during the course of Ann's preparation of Charlie's tax returns, for advice on how he should allocate certain of his assets. Ann suggests that Charlie diversify his investments among real estate, bonds, and mutual funds. Ann charges for this advice on an hourly basis, at the same hourly rate she charges Charlie for accounting and tax services. In this case, Ann seems to be holding herself out to the public as a financial planner, and Ann probably would need to register as an investment adviser.

2. Bill is a CPA who publishes a newsletter sent to all of his clients that regularly lists specific stocks that Bill believes are a good investment. Bill does not charge for the newsletter and its cost is not directly factored into his hourly rate for accounting services. While Bill isn't explicitly holding himself out to the public as an investment adviser, he clearly is giving investment advice in the monthly newsletter, and the "holding out" requirement may be satisfied if that type of advice is a regular feature of the newsletter. Nevertheless, because Bill is not charging for the advice, Bill may argue that he is not required to register as an investment adviser. If the newsletter contained a referral to an investment adviser who pays Bill a referral fee for new clients, the "compensation" requirement may be satisfied, requiring Bill to register as an investment adviser. (Even if Bill were not otherwise deemed to be an investment adviser, the payment of the referral fee will subject Bill to the "solicitors rule," discussed in Appendix 1).

3. Catherine is a CPA who has obtained the Personal Financial Specialist (PFS) credential from the AICPA. On her letterhead under her name are the words "Certified Public Accountant—Personal Financial Specialist." Catherine regularly advises clients that their

assets should be diversified among various categories, including real estate, stocks, bonds, and mutual funds, with recommendations for specific allocations in each asset category tailored for each client. Catherine charges for this advice on an hourly basis. Because it appears that Catherine is holding herself out as an investment adviser, and because her investment advisory services do not appear to be incidental to her accounting services but rather an integral part of her business, Catherine probably will need to register as an investment adviser.

4. Dave is a CPA who publishes a newsletter that recommends individual stocks. He sends the newsletter only to those clients of his accounting firm who subscribe and pay a $300 annual subscription fee. Dave also has a handful of subscribers to his newsletter who are not clients of his accounting firm. Because the investment advisory services are not incidental to his accounting services, and because he receives compensation for the investment advisory services, Dave probably will need to register as an investment adviser.

5. Eleanor is a CPA who utilizes a software program that summarizes the performance of mutual funds over various periods, categorizes funds by objective, performance, sales charges, and risk levels; to inform accounting clients about mutual funds, provides them with a list of funds that meet their investment objectives; and provides monthly performance reports. Eleanor charges each client who asks for advice on mutual fund investments a fee of $250 per quarter to render a report generated by the software. Because Eleanor is holding herself out to the public as providing financial planning services, and because she appears to be providing investment advice for a fee, Eleanor probably will need to register as an investment adviser.[30]

6. Fred is a CPA who advertises on his website that he provides "accounting and investment consulting." From time to time, Fred will, for a fee, assist clients who are considering investing in real estate limited partnerships by discussing with them the merits and risks of investing in the limited partnership, including advising on the past performance of the general partner in similar partnerships. Because Fred is holding himself out to the public as providing investment-related services, and because he is rendering advice for compensation on securities (limited partnership interests) as a regular part of his business, Fred probably will need to register as an investment adviser.[31]

7. Gloria is a partner in an accounting firm that includes ten other CPAs. Gloria and one of her partners, Hank, have both obtained their PFS credential from the AICPA. The firm's partners want to take advantage of Gloria's and Hank's financial planning expertise as a new profit center for the firm. However, if Gloria and Hank provide financial planning services that include advice on the pros and cons of investing in securities, the firm probably would need to register as an investment adviser. If, instead, the firm forms a new entity through which Gloria and Hank will provide those same services, and the accounting firm neither holds itself out as providing investment services nor actually performs such services, only the new entity probably will need to register as an investment adviser.

[30] See Hungerford, Aldrin, Nichols & Carter, SEC No-Action Letter, 1991 WL 290535 (Dec. 10, 1991).
[31] See Jan L. Warner, SEC No-Action Letter (Dec. 27, 1988).

8. Henry is a CPA who is employed by the Rich Family Office to provide tax, estate planning and accounting services to members of the Rich family. As part of his duties, Henry selects investment advisers to manage the securities portfolios of Rich family members and monitors the performance of the managers and the portfolios. Although Henry is employed to provide services that include advice concerning securities, he is providing the advice through a family office that has only single family clients, so he may rely on the family office exclusion from the investment adviser definition.

9. Irene is a CPA who offers accounting and tax services through her accounting firm. One of her clients is the Mula Family Office. The head of the family office occasionally asks Irene to review private equity, venture capital, real estate, and other private funds for possible investment by Mula family members and trusts. Irene charges her regular hourly fee for these services. Irene cannot rely on the family office exclusion for providing these services because she is not a director, partner, member, manager, or employee of the Mula Family Office and probably will need to register as an investment adviser.

10. Jerry is a CPA employed by the Jones Family Office, where he provides investment management services. From time to time, Jerry is asked to provide investment advice to persons outside the Jones family who do not pay for the advice. While the SEC has not formally agreed or disagreed, Jerry can argue that providing those services without compensation to persons who are not family clients should not prevent reliance on the family office exclusion and that he is not required to register as an investment adviser.

Where Do I Register?

If you need to register as an investment adviser, you generally will need to make your primary registration either with the SEC or with one or more states. If you register with the SEC, certain other filings may be required in various states.

Do I Need to Register with the SEC?

The Dodd-Frank Act changed the eligibility requirements for determining whether an adviser is required to register with the SEC or a state regulator. If you have $100 million or more in assets under management, you are generally required to register with the SEC. If you have assets under management of between $25 million and $100 million (a "midsized" adviser) or less than $25 million (a "small" adviser), you generally are not permitted to register with the SEC and instead will register with one or more states, unless an exemption applies.[32] State registration is discussed in Section IV.B below.

There are several exemptions to the prohibition on advisers with less than $100 million in assets under management registering with the SEC.[33] For instance:

- Advisers with a principal office and place of business in a state in which they are not regulated or required to be regulated must register with the SEC. Wyoming is the only state without an investment adviser statute.

[32] See Advisers Act § 203A, 15 U.S.C. § 80b-3a and Advisers Act Rule 203A-1, 17 C.F.R. § 275.203A-1.
[33] See Advisers Act § 203A, 15 U.S.C. § 80b-3a and Advisers Act Rule 203A-2, 17 C.F.R. § 275.203A-2.

- Midsized advisers (assets under management [AUM] between $25 million and $100 million) with a principal office and place of business in a state in which they are not required to be registered or, if registered, would not be subject to examination, may register with the SEC. New York and Wyoming do not examine advisers registered with them.

A key issue in determining filing requirements is the dollar amount of securities under management. Even if you don't "supervise" or "manage" client securities, if you render advice about securities to a client for compensation on anything other than rare, isolated, and nonperiodic instances, you may still need to register with a state.

HOW DO I CALCULATE REGULATORY ASSETS UNDER MANAGEMENT?

Your regulatory AUM is determined by calculating the **securities portfolios** for which you provide **continuous and regular** supervisory or management services as reported on Form ADV. Instructions for Part 1A of Form ADV explain how to complete Item 5.F, "Regulatory Assets Under Management." (Form ADV and Instructions can be found at www.sec.gov/about/forms/formadv.pdf.)

There are three questions to ask when calculating regulatory assets under management. First, is the account a securities portfolio? Second, does the account receive continuous and regular supervisory or management services? Third, what is the entire value of the account?

What Is a Securities Portfolio?

An account is a securities portfolio if at least 50% of the total value of the account consists of securities.[34] For purposes of this test, cash and cash equivalents may be treated as securities. The following portfolios must be included when calculating the investment adviser's regulatory assets under management: family or proprietary accounts, accounts for which no compensation is received for services provided, and accounts for non–U.S. resident clients.[35]

What Does "Continuous and Regular Supervisory or Management Services" Mean?

The Instructions for Part 1A of Form ADV provide general criteria and factors to consider when evaluating whether you provide continuous and regular supervisory or management services to an account. In general, you provide continuous and regular supervisory or management services if

- you have discretionary authority over and provide ongoing supervisory or management services with respect to the account; or
- you do *not* have discretionary authority over the account, *but* you have ongoing responsibility to select or make recommendations, based upon the needs of the client, as to specific securities or other investments the account may purchase or sell and, if such recommendations are accepted by the client, you are responsible for arranging or effecting the purchase or sale.

[34] Form ADV: Instructions for Part 1A, Item 5.F.
[35] Id.

The following factors should be considered when evaluating whether you provide continuous and regular supervisory or management services to an account:[36]

- Terms of the advisory contract—if you agree in an advisory contract to provide ongoing management services; it suggests that you are providing these services for the account.
- Form of compensation—compensation based on the average value of your client's assets over a period of time (for example, 1% of the assets under management over a six-month period) suggests that you are providing continuous and regular supervisory or management services. Compensation based on the time spent with your client during a client visit, or a retainer based on a percentage of assets covered by a financial plan, suggests you do *not* provide continuous and regular supervisory or management services.
- Management practices—do you actively manage assets or provide advice? Infrequent trades alone do not mean that the services you provide are not continuous and regular.

What Is the Value of the Account?

An account is a securities portfolio if at least 50% of the total value of the account consists of securities. So long as at least 50% of the total value of the account consists of securities, cash, and cash equivalents, the entire value of the account is included in the "regulatory assets under management" calculation.[37]

STATE NOTICE FILING REQUIREMENTS

SEC-registered investment advisers have a filing obligation, known as a notice filing, in states where the investment adviser does business. All states except Wyoming require SEC-registered investment advisers providing investment advice in that state to make a notice filing with the state.[38] Generally, this notice filing obligation is imposed if within the preceding 12-month period the investment adviser had a place of business in the state and six or more clients who are residents of the state, but not all states have the same requirements or obligations.[39] Notice filings are submitted to the states through the Investment Advisers Registration Depository[40] (IARD) and typically consist of copies of the documents that are filed with the SEC. The IARD is discussed in Section V below.

State Registration

Investment advisers with assets under management of less than $100 million are subject to registration with the state securities regulator in each state. In most states, the definition of an investment adviser is identical to the definition in the Advisers Act, but you should consult with the state securities administrator or your lawyer or compliance advisor on any particular state's requirements.

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[36] Form ADV: Instructions for Part 1A, available at www.sec.gov/about/forms/formadv.pdf.
[37] Id.
[38] Id. Technically, the "notice filing" is a means of providing a state with notice that an SEC-registered investment adviser is doing business in that state. A notice filing is not the same as "registering" as an investment adviser under that state's investment adviser registration statute. See "State Registration," *infra*.
[39] See Section IV.B.1. of this Guide.
[40] Form ADV, Part 1, Item 2.C.

State registration requirements are generally similar, but not uniform. Many states have registration procedures similar to the SEC's procedures and permit filing of the Form ADV instead of a separate state form. Some states require advisers to file supplemental forms containing additional information, such as advisory contracts, financial statements, and the like. In general, all states accept filing of Form ADV through the IARD system.[41]

In general, an investment adviser subject to state-regulation will need to register with each state in which it operates and will need to familiarize itself with the registration and regulation requirements of each such state.[42] However, a state-registered investment adviser need only comply with the recordkeeping, net capital, and bonding requirements of the state in which the adviser maintains its principal office and place of business. The Advisers Act prohibits other states in which the investment adviser is registered from imposing more burdensome requirements.[43]

The State registration process will vary from state to state and is beyond the scope of this Guide. A CPA seeking state registration should consult counsel and check the current requirements directly with each state in which it plans to register. A complete list of state securities regulators is available at www.nasaa.org/about-us/contact-us/contact-your-regulator.

DO I NEED TO REGISTER WITH A STATE IF I HAVE FEWER THAN FIVE CLIENTS IN THAT STATE?

Generally, if a CPA does not have a place of business in the state, he is allowed up to five investment advisory clients before he must register. This is commonly known as the *de minimis* exemption from registration.[44] However, some states require a filing before you can conduct an advisory business in that state even if you have only one client.[45] You should check individual state requirements.

Investment Adviser Representative Registration

States may also require registration or qualification of investment adviser representatives who have a place of business located within that state.

An "investment adviser representative" is a supervised person[46] of the investment adviser who has more than five clients who are natural persons (subject to certain exceptions) and more than 10% of whose clients are natural persons.[47] An investment adviser representative does *not* include a supervised person who does not, on a regular basis, solicit or communicate with clients or who provides only impersonal investment advice.

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[41] Regulation of Investment Advisers § 1:68.
[42] Form ADV, Part I, Item 2.C.
[43] Advisers Act § 222, 15 U.S.C. § 80b-18a.
[44] Advisers Act § 222(d), 15 U.S.C. § 80b-18a(d).
[45] As of July 2012, Louisiana, Nebraska, New Hampshire, and Texas require notice filings before conducting any investment advisory business in the state.
[46] See Attachment 3 Definitions, *infra*. "Supervised person" is a partner, officer, director, or employee of an investment adviser, or other person who provides investment advice on behalf of the investment adviser and is subject to supervision and control of the adviser. Advisers Act § 202(a)(25), 15 U.S.C. § 80b-2(a)(25).
[47] Advisers Act Rule 203A-3(a)(1), 17 C.F.R. § 275.203A-3(a)(1).

An individual employed or associated with an investment adviser who does any of the following would likely be considered an investment adviser representative:

- Makes any recommendations or gives investment advice regarding securities;
- Manages accounts or portfolios of clients;
- Determines which recommendation or advice regarding securities should be given;
- Provides investment advice;
- Solicits, offers, or sells investment advice for compensation; or
- Supervises employees who perform the foregoing.[48]

In addition, most states require investment adviser representatives to pass either a Series 65 (North American Securities Administrators Association [NASAA]—Uniform Investment Adviser Law) or Series 66 (NASAA—Uniform Combined State Law) examination, although many states exempt persons who have received the Certified Financial Planner, Chartered Financial Analyst, Chartered Financial Consultant, or Chartered Investment Counselor certifications or who are CPAs with a Personal Financial Specialist designation.[49]

Switching to or from SEC/State Registration

As a result of the Dodd-Frank Act, midsized advisers (AUM between $25 million and $100 million) who were registered with the SEC on January 1, 2012, were required to withdraw from SEC registration and transition to state registration by June 28, 2012, unless (i) the adviser is an investment adviser to a registered investment company (mutual fund), (ii) the adviser has a principal office and place of business in a state in which it is not required to be registered or, if registered, would not be subject to examination (New York and Wyoming), (iii) the adviser would be required to register with 15 or more states, or (iv) the adviser can rely on another exemption to the prohibition on SEC registration.[50]

SEC rules also provide a buffer for midsized advisers with close to $100 million of assets under management to determine whether and when to switch between SEC and state registration. A mid-sized adviser must register with the SEC if it has $110 million of assets under management, but once registered with the SEC, an adviser need not withdraw its registration until it has less than $90 million of assets under management.[51]

How Do I Apply For Registration?

FINRA, working with the SEC and NASAA, has developed and operates an online system for the registration of investment advisers called the IARD. Form ADV Part 1A and the brochure required by Form ADV Part 2A must be filed electronically through IARD.

[48] Uniform Securities Act (2002) §102(16).
[49] Regulation of Investments Advisers § 1:66.
[50] See Section IV.A. of this Guide.
[51] Advisers Act Rule 203A-1(a)(1), 17 C.F.R. § 275.203A-1(a)(1).

How Do I Get Access to IARD?

The forms, called the Entitlement Packet, and other information about setting up an IARD account are available at www.iard.com. On the left side of the screen, click on "How to Access IARD" and print an SEC Adviser Entitlement Packet or State Registrant Entitlement Packet, as applicable. Firms request access to IARD by completing and submitting the Super Account Administrator (SAA) form to FINRA. Instructions for where and how to submit the form are provided in the Entitlement Packet.

After the SAA Entitlement Form is submitted, FINRA will set up the IARD user account for the investment adviser, grant access to the individuals the investment adviser designated as Authorized Persons so these persons can make electronic filings on your behalf, and will set up the IARD financial account for billing and payment of fees. FINRA will send the investment adviser confirmation e-mails containing a user ID and password, with a link to instructions on electronic filing through IARD and payment of fees collected by IARD.

The SEC and the states impose filing fees for registration of the firm. Fees are paid to FINRA and disbursed to each regulatory authority. Funds may be submitted by check or wire transfer to your IARD billing account. Allow 48 hours for the processing of funds. Once funds are credited to your IARD account, you can submit the electronic filing.[52]

Filing Form ADV

Form ADV is the investment adviser's application for registration. Form ADV contains four parts.

Part 1A asks a number of questions about the investment adviser, the adviser's business practices, the persons who own and control the adviser, and the persons who provide investment advice on behalf of the adviser.

- All advisers registering with the SEC or any state must complete Part 1A.
- A business entity, such as a corporation, limited liability company, or partnership, rather than an individual, often operates as the investment adviser. In that event, it is important that the Form ADV be completed to reflect this fact. [53]

Part 1B asks additional questions required by state securities authorities. If applying for SEC registration, Part 1B need not be completed.

Part 2A requires advisers to create a narrative brochure containing information about the advisory firm. The requirements of Part 2A apply to all investment advisers registered with or applying for registration with the SEC.

[52] FINRA also uses Web E-Pay, which allows an investment adviser to authorize electronic payments directly from a designated bank account to the investment adviser's Daily and/or Renewal accounts. You can access Web E-Pay from the IARD website, www.IARD.com, by clicking on "Web CRD/IARD E-pay," located on the left side of the screen.

[53] Regulation of Investment Advisers §1:56.

Part 2B requires advisers to create brochure supplements containing information about certain supervised persons. The requirements of Part 2B apply to all investment advisers registered with or applying for registration with the SEC. [54]

- The SEC permits advisers to list the professional designations held by such persons. Any listing of professional designations held must provide a sufficient explanation of the minimum qualifications required for the designation to allow clients and potential clients to understand the value of the designation.

- The AICPA has prepared descriptions of the CPA license and PFS credential as guidance to its members who choose to list their professional designations on Part 2B. These descriptions are in Appendix 5 to this Guide.

A copy of Form ADV is in Appendix 6 to this Guide. You can also access a version of Form ADV on the Internet at www.sec.gov/about/forms/formadv.pdf.

The Advisers Act, specifically Section 207, makes it unlawful for an applicant to make an untrue statement of material fact or to willfully omit a material fact in any registration application or report filed with the SEC. It is extremely important to complete Form ADV fully and accurately.[55]

What Are the Filing Fees?[56]

There are two fees for SEC registration—an initial set-up fee and an annual fee. The initial set-up fee is charged when the investment adviser submits its first electronic Form ADV. The annual fee is charged at the time the investment adviser submits its Annual Amendment, which is due within 90 days after the end of the investment adviser's fiscal year. The amount of the fees depends on the value of the investment adviser's assets under management, as follows:[57]

Assets Under Management	Initial Set-Up Fee	Annual Fee
SEC under $25 million	$40	$40
SEC $25–$100 million	$150	$150
SEC over $100 million	$225	$225

There are also IARD system fees assessed for electronic filing of forms for investment adviser registration on the IARD system.

When Does the SEC Approve My Registration?

The investment adviser's application, Form ADV Part 1A and Part 2A brochure, is deemed filed as of the date that you successfully submit it through IARD.[58] The SEC will then review your Form ADV materials to determine whether they are complete and in compliance with the Advisers Act. The SEC will grant registration, or institute a proceeding to determine whether an

[54] Form ADV: General Instruction 3.
[55] See Regulation of Investment Advisers §1:57.
[56] See www.iard.com/fee_schedule.asp and www.sec.gov/divisions/investment/iard.shtml.
[57] These are the fees in effect as of January 2012. Fees change from time to time.
[58] Regulation of Investment Advisers §1:58.

application should be denied, within 45 days of filing the completed Form ADV.[59] If your application is approved, you will receive an order from the SEC that evidences effective registration.

What Are My Duties As An Investment Adviser?

Investment advisers are *fiduciaries* to their clients. In other words, investment advisers have a fundamental obligation to act in the best interests of the client and to provide investment advice that is in the client's best interests.

What Does It Mean to Be a Fiduciary?

As a fiduciary, the investment adviser has an affirmative duty of utmost good faith to act solely in the best interests of the client and to make full and fair disclosure of all material facts.[60] Disclosure is particularly important when the interests of the investment adviser and the interests of the client may come into conflict.

The SEC has identified specific obligations resulting from the fiduciary duty the investment adviser owes its clients which include, but are not limited to: (1) a duty to have a reasonable independent basis for its investment advice; (2) a duty to obtain the best execution for clients' securities transactions where the adviser is in a position to direct brokerage transactions; (3) a duty to ensure that its investment advice is suitable to the client's objectives, needs and circumstances; (4) a duty to refrain from effecting personal securities transactions inconsistent with client interests; and (5) a duty to be loyal to clients.[61]

The fiduciary duty an investment adviser owes its clients is a key legal difference between an investment adviser and a broker-dealer. A broker-dealer or a registered representative of a broker-dealer is not a fiduciary when rendering investment advice in connection with executing securities transactions for its clients; rather, the investment recommended must merely be suitable to the client.

The Dodd-Frank Act required the SEC to conduct a study on the effectiveness of existing standards of care for broker-dealers, investment advisers, and their representatives. The 2011 study by the SEC staff recommended the SEC adopt and implement a uniform fiduciary standard of conduct for broker-dealers and investment advisers—no less stringent than that currently applied to investment advisers—when those financial professionals provide personalized investment advice about securities to retail investors.[62] The AICPA's PFP Executive Committee supports this elevated standard of care.

[59] Id. at §1:61. The 45-day period may be longer if the applicant consents.
[60] Regulation of Investment Advisers §2:33.
[61] Regulation of Investment Advisers §2:33 (internal citations omitted).
[62] Study on Investment Advisers and Broker-Dealers As Required by Section 913 of the Dodd-Frank Wall Street Reform and Consumer Protection Act by the Staff of the U.S. Securities and Exchange Commission (January 2011).

Compliance

The Advisers Act and the Rules thereunder contain numerous provisions relating to compliance including, but not limited to, disclosure requirements, requirements relating to custody of client assets, recordkeeping requirements, and permissible advertising. Investment advisers need to be aware of and follow these requirements. Violations of the Advisers Act or its Rules may give rise to disciplinary proceedings, monetary penalties, and/or criminal penalties.[63] Information relating to disciplinary proceedings at the very least can prove embarrassing for an investment adviser, as disciplinary information is publicly available.[64]

Disclosure. Registered investment advisers are required to deliver certain written disclosure to clients or prospective clients containing the information required by Part 2 of Form ADV.[65]

Form ADV Part 2 consists of a series of items that contain disclosure requirements for the investment adviser's written disclosure statement, referred to as a "brochure," that provides information about the investment adviser's background, business practices, advisory services provided, fees, investment strategies, risks, disciplinary information, financial industry affiliations, brokerage and trading practices, custody, investment discretion, proxy voting, conflicts of interest, and material changes from the last annual update. The items require narrative responses in the same order as they appear in the form to promote uniformity and comparison among advisers, and must be written in plain English, taking into consideration the adviser's clients' level of financial sophistication. Investment advisers are also required to deliver "brochure supplements" for certain advisory personnel.

Custody. Registered investment advisers who have custody of client assets are required to maintain those assets with a qualified custodian (bank or broker-dealer), provide specified notice to clients, and undergo a surprise examination by an independent public accountant once a year to verify client assets, subject to certain exceptions.[66] "Custody" means holding client funds or securities, or having authority to obtain possession of them. Custody includes:

- Possession of client funds or securities (but not of checks drawn by clients made payable to third parties) unless received inadvertently and promptly returned;
- Any arrangement (including a general power of attorney) under which you may withdraw client funds or securities maintained with a custodian upon your instruction; and
- Any capacity (such as a general partner of a limited partnership, managing member of a limited liability company, or trustee of a trust) that gives you or your supervised person legal ownership or access to client funds or securities.

Registered investment advisers who have custody of client funds or securities solely because of their authority to deduct advisory fees from client accounts are not required to have an annual independent verification.

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[63] Advisers Act §203(e), 15 U.S.C. §80b-3(e) (disqualification provisions); Advisers Act §203(i), 15 U.S.C. §80b-3(i) (monetary penalties); Advisers Act §217, 15 U.S.C. §80b-17 (criminal penalties).
[64] See Investment Adviser Public Disclosure website, available at:www.adviserinfo.sec.gov/IAPD/Content/IapdMain/iapd_SiteMap.aspx.
[65] Advisers Act Rule 204-3, 17 C.F.R. §275.204-3.
[66] Advisers Act Rule 206(4)-2, 17 C.F.R. §275.206(4)-2.

Recordkeeping. Registered investment advisers are required to maintain the following books and records relating to its investment advisory business:[67]

- A journal (including cash receipts and disbursements records) and other records of original entry forming the basis of any ledger entries.
- General and auxiliary ledgers or comparable records reflecting asset, liability, reserve, capital, income, and expense accounts.
- A memorandum of each order given by the adviser, or any instruction received from the client, concerning the purchase, sale, receipt or delivery of a security, showing the terms and conditions of the order, instruction, modification or cancellation, who recommended the transaction, who placed the order, the account for which entered, date of entry and bank or broker dealer through whom executed, with discretionary orders so designated.
- All check books, bank statements, cancelled checks, and cash reconciliations of the adviser.
- All bills or statements relating to the advisory business.
- All trial balances, financial statements and internal audit work papers relating to the advisory business.
- All written communications received or sent by the adviser relating to any recommendation or advice, receipt or disbursement of funds or securities, or placing or executing any order, subject to certain exceptions.
- List of all discretionary client accounts.
- All powers of attorney or other documents granting discretionary authority by a client.
- All written agreements with clients or relating to the advisory business.
- Each notice, circular, advertisement, article, investment letter, bulletin, or other communication distributed to 10 or more persons and the reasons for any recommendation of specific securities made in the communication.
- The adviser's code of ethics, record of any violation, and action taken.
- Personal securities holdings and transactions reports by adviser personnel.
- Each brochure, brochure supplement and amendments, method of computing managed assets and descriptions of legal or disciplinary events under certain circumstances, and written acknowledgement of client receipt of brochures and supplements.
- All accounts, books, internal work papers, and other records necessary to demonstrate the calculation of performance or rate of return for managed accounts or securities recommendations in any communication.

[67] Advisers Act Rule 204-2, 17 C.F.R. §275.204-2.

- Written policies and procedures concerning compliance with the Advisers Act and rules.

The books and records required to be kept by advisers having custody or possession of client securities or funds must include:

- A journal of all purchases, sales, receipts, and deliveries of securities for, and all other debits and credits to, such accounts.
- A separate ledger for each such client showing all purchases, sales, receipts and deliveries, date and price of each purchase or sale, and all debits and credits.
- Copies of confirmations of all transactions for such clients.
- Position listing for each security showing name of client, amount, and location of security.

Advisers who render investment supervisory or management services, or who exercise voting authority with respect to client securities, are required to maintain additional records related to those activities.

All books and records required to be maintained by registered investment advisers must be maintained for at least five years, except for the adviser's organizational documents, which must be kept until at least three years after termination of the enterprise. All required books and records may be maintained on micrographic media (microfilm or microfiche) or in electronic storage media (if safeguarded from loss, alteration, or destruction, with access limited to properly authorized personnel).

Advertising. The SEC regulates advertisements by registered and unregistered investment advisers.[68] An advertisement is broadly defined to include any notice, circular, letter, or other written communication, or any announcement in a publication, by radio or television, that offers any analysis, report, or publication concerning securities; that is used to determine when or which securities to buy or sell; or that offers any other investment advisory service concerning securities.

Registered investment advisers are prohibited from using any advertisement that:[69]

- Refers to any testimonial concerning the adviser or its investment advice or services;
- Refers to past specific recommendations that were profitable, unless the advertisement shows or offers to furnish a list of all recommendations by the adviser within at least the previous one-year period and the advertisement contains specified information about the recommended security and cautionary language;
- Represents that a graph, chart, formula, or other device offered can by itself be used to determine which securities to buy or sell, when to buy or sell them, or that the device will provide assistance in making such decisions unless the advertisement prominently discloses the limitations and difficulties in using the device;

[68] Advisers Act §206(4), 15 U.S.C. §80b-6(4).
[69] Advisers Act Rule 206(4)-1, 17 C.F.R. §275.206(4)-1.

- Represents that any report or services will be furnished free or without charge unless actually so furnished; or
- Contains any untrue statement of a material fact or is otherwise false or misleading.

Performance advertising is not *per se* fraudulent under the Advisers Act, but is evaluated under a "fact and circumstances" test. The SEC staff has stated that the following practices are misleading in connection with using model or actual performance results:[70]

- Failing to disclose the effect of material market or economic conditions on the results portrayed.
- Failing to reflect the deduction of advisory fees, brokerage commissions, and other expenses the client would have paid.
- Failing to disclose whether and to what extent the results portrayed include the reinvestment of dividends and other earnings.
- Suggesting potential profits without also disclosing the possibility of loss.
- Comparing results to an index without disclosing all material factors relevant to the comparison.
- Failing to disclose any material conditions, objectives, or investment strategies used to obtain the performance advertised.

The use of performance data in advertising in compliance with the Advisers Act can be challenging and potentially problematic. It is important to carefully review the restrictions set out in the SEC no-action letters in this area.[71]

Other Compliance Obligations. Other ongoing compliance obligations may include:

- Providing disclosure and financial statements to clients
- Bonding
- Examinations and qualifications
- Photographs and fingerprints
- Limits on advisory fees
- Limits on advertising and certain business practices
- Restrictions on custody of client assets
- Principal or agency cross transactions
- Limits on wrap fees
- Avoiding conflict of interest situations
- Restrictions on sharing advisory compensation
- Licensing of representatives
- Continuing education
- Record retention
- Maintaining customer complaint files
- Capital or financial adequacy
- Customer background documentation
- Guidelines on electronic communication and Internet use
- Drafting a code of ethics
- Compliance policies and procedures

[70] Clover Capital Management, Inc., SEC No-Action Letter, 1986 WL 67379 (Oct. 28, 1986).
[71] See Regulation of Investment Advisers §§2.69-2.87 and the no-action letters cited and discussed.

Regulatory Examinations. Investment advisers registered with the SEC are subject to examination by the SEC, while advisers registered at the state level are subject to examination by state regulatory authorities. The primary purposes of such examinations are to determine whether the adviser is in compliance with the Advisers Act and other applicable federal and state securities laws and that the adviser's business activities are consistent with the information disclosed in the adviser's Form ADV.[72]

Professional Considerations

As a CPA, you are regulated by your state board of accountancy, which has the authority to impose sanctions for certain violations. If you are a member of the AICPA, you must abide by the AICPA Code of Professional Conduct (the Code) that sets forth certain standards of professional conduct. These professional standards are in addition to federal and state securities regulatory requirements.

Objectivity, Integrity, and Disclosure

Under the Code, in the performance of any professional service, a member must maintain objectivity and integrity, shall be free of conflicts of interest, and shall not knowingly misrepresent facts.

A conflict of interest may occur if a member performs a professional service for a client, and the member or his or her firm has a relationship with another person, entity, product, or service that could, in the member's professional judgment, be viewed by the client or other appropriate parties as impairing the member's objectivity. The following are some examples (not intended to be exhaustive) of relationships that could be viewed as impairing the member's objectivity:

- In connection with a PFP engagement, an accountant plans to suggest that the client invest in a business in which the accountant has a financial interest.
- An accountant has provided tax or PFP services for a married couple who are undergoing a divorce, and the accountant has been asked to provide the services for both parties during the divorce proceedings.
- A member refers a PFP or tax client to an insurance broker or other service provider, who then refers clients to the accountant under an exclusive arrangement to do so.

If you are involved in a conflict of interest situation or even a potential conflict of interest situation, you must disclose the conflict or potential conflict to your clients who are affected and must obtain their consent.

Review the AICPA Code of Professional Conduct for more information.

[72] Regulation of Investment Advisers §2:208.

Independence and Conflicts of Interest

Accountants in public practice should be independent in fact and appearance when providing auditing and other attestation services. If you provide attestation or assurance services to clients, a conflict of interest may prevent you from also providing investment advisory services (IAS).

AICPA rules state that an accountant's independence will be impaired if the accountant	**Accountants may provide certain advisory services to audit clients without impairing independence. Accountants can**
• Makes investment decisions on behalf of audit clients or otherwise has discretionary authority over an audit client's investments; • Executes a transaction to buy or sell an audit client's investment; or • Has custody of assets of the audit client, such as taking temporary possession of securities purchased by the audit client.	• Recommend the allocation of funds that an audit client should invest in various asset classes, based on the client's risk tolerance and other factors. • Provide a comparative analysis of the audit client's investments to third-party benchmarks. • Review the manner in which the audit client's portfolio is being managed by investment managers. • Transmit an audit client's investment selection to a broker-dealer, provided the client has made the investment decision and authorized the broker-dealer to execute the transaction.

Commissions and Referral Fees

The Code prohibits the receipt of third-party commissions and referral fees under certain circumstances. An accountant cannot refer a product or service to a client for a commission if the accountant or his or her firm also performs audit, review, or compilation services or examines prospective financial information for the client. An accountant who receives a permitted commission or referral fee must disclose the commission or fee to the client.

Review the AICPA Code of Professional Conduct for more information.

High Standard of Care

A fiduciary has a legal duty to act solely in the best interests of the beneficiary. Although an accountant normally is not considered to be a fiduciary to his or her clients, the Code embodies standards of conduct that are closely analogous to a fiduciary relationship: objectivity, integrity, free of conflicts of interest, and truthfulness. Accountants who provide audit services cannot be held to a fiduciary standard, given their duty to the public.

Courts have found that an accountant can be a fiduciary to his or her client when providing certain professional services, including tax services, asset management, and general business consulting. Generally, if the following three elements are present in a client relationship, an accountant may be deemed to be a fiduciary to his or her client: (*a*) the accountant holds himself or herself out as an expert in an aspect of business, (*b*) the client places a high degree of trust and

confidence in the accountant, and (*c*) the client is heavily dependent upon the accountant's advice. An accountant who provides IAS as a registered IA is a fiduciary to his or her advisory clients.

To help you in understanding and implementing a prudent investment process, the AICPA and the Fi360 developed a series of guides for investment fiduciaries, including *Prudent Practices for Investment Advisors*.

Conclusion

In delivering PFP services, you face legal and regulatory issues different from those of auditing, accounting or tax services. The business model you select for providing investment services—investment adviser, investment adviser representative, solicitor, or registered representative—will determine the legal and regulatory issues applicable to you. The most common model used by CPAs engaging in or seeking to add PFP services is the investment adviser model.

Whether a CPA who provides investment advice must register as an investment adviser with the SEC or with one or more states depends on a number of factors, including whether the CPA is in the business of providing advice about securities for compensation and whether that advice is incidental to his or her accounting practice. This analysis depends on the facts and circumstances of each case. Because possible civil and criminal penalties can be imposed on the failure to register, you should seek legal counsel or compliance advisor to assist you in making the determination of whether registration is required.

This Guide is intended to provide you with a general understanding of common business models for CPAs in providing investment services, the issues surrounding the determination of whether registration as an investment adviser is necessary, a general overview of how and where to register, and a general explanation of your duties as an investment adviser. Please keep in mind that questions you may have should be directed to your legal counsel or compliance advisor. This Guide is not intended to be a substitute for legal advice.

Appendix 1 – Business Model Table

Type	Registered Investment Adviser (RIA)	Investment Adviser Representative (IAR)	Referral/Solicitor's Agreement	Registered Representative (RR) of a Broker/Dealer
Description	An investment adviser provides advice to clients about investing in securities for a fee (rather than a commission).	An investment adviser representative provides investment advice to clients on behalf of a RIA.	A solicitor "finds" and refers clients to a financial services professional for a fee.	A registered representative is licensed to sell securities for a broker-dealer.
Specifics	This model may be appropriate for a CPA who wants more freedom and control over the services offered to clients. With this model, the CPA firm establishes and registers as an independent RIA. The RIA would need to maintain the operational side of the practice (for example, investment research, administrative, and compliance functions) by having its own "back-office" operation. The RIA would then work directly with a custodian, such as Fidelity, Schwab, and Pershing LLC, among others, and use a clearing house. Alternatively, the RIA can have a service agreement with one or more broker-dealers that are used on behalf of clients. The broker-dealer can also provide some of the administrative support. The CPA firm must register as an RIA with either the applicable state(s) or the SEC. If registered with the SEC, additional state requirements may apply. This model allows independence and retention of revenues but requires development of your own "back-office" and support services. The CPA manages a client's portfolio, either making specific investment decisions or establishing alliances with money managers to perform some or all money management functions.	This model may be appropriate for a CPA who wants to offer fee-only services and who wants the support of an RIA firm or a broker-dealer's RIA (collectively, RIA). With this model, your firm will typically participate in an RIA's fee-only advisory program and receive a share of the fees charged to clients. The payout generally varies depending on many factors, such as the level of support provided. The CPA firm may be required to pay administrative or other fees to the RIA. The CPA firm's employees must be registered as IARs. (The firm must determine if the state requires a Series 65 examination. Personal Financial Specialist [PFS] and Certified Financial Planner [CFP] examinations are accepted in lieu of the Series 65 exam in most states.) RIAs and IARs are subject to a fiduciary duty. Under this standard, the IA must put the client's interest ahead of his or her own at all times and must provide advice and recommendations that he or she views as being the best for the client. IAs are also required to provide upfront disclosures, including whether there are any possible conflicts of interest.	This model may be appropriate for a CPA firm that does not want to make a large capital investment or build the investment expertise in house. With this model, the CPA firm refers clients to an RIA or RR in return for a percentage of the RIA's or RR's management fee (referral fee). The CPA does not make specific investment decisions. The fee may be one time or ongoing (for example, 25 percent of RIA's quarterly fee). CPAs may need to get licensed and registered to share commissions and fees. It is recommended that you consult with a securities attorney with expertise in the area before making any final decisions about legal issues, such as compliance, registrations, or exemptions. Care must be taken so the CPA does not cross the line from finding clients for an RIA to serving as an IA. The RIA, not the CPA firm, has control and responsibility over management of the client's portfolio, although the CPA, under other requirements, is ultimately responsible for the services. SEC rules require a written agreement between the RIA and solicitor, and delivery to the client of the RIA's brochure and a separate solicitor's brochure describing the RIA/solicitor relationship and solicitor	This model may be appropriate for an individual who wants commission-based compensation and the support of a larger organization. With this model, your firm will directly affiliate with a FINRA member broker/dealer. Your employees must be licensed to sell securities (generally must have Series 6 or Series 7 and Series 63 registrations). Additional registration requirements may apply (such as registering as an IA), and the broker-dealer may share in advisory fees. The RR may be an employee or independent contractor of the broker-dealer. As an agent of the broker-dealer, the CPA is subject to the broker-dealer's supervision and can only sell products and conduct business authorized by the broker-dealer. Broker-dealers are subject to a suitability standard (that is, they are required to know the client's financial situation well enough to understand his or her financial needs and to recommend investments for the client that are appropriate for him or her based upon that knowledge). The CPA firm's "payout" would depend on the volume of business and how much support is provided by the broker-dealer. You can choose to work on a commission or fee basis with clients. The broker-dealer for your office provides services, including trading and operations; product and market research; and accounting, marketing, compliance, training, and advisory services.

Type	Registered Investment Adviser (RIA)	Investment Adviser Representative (IAR)	Referral/Solicitor's Agreement	Registered Representative (RR) of a Broker/Dealer
			compensation.	
Pros	♦ The CPA and client interests are better aligned. ♦ The CPA can control and strengthen the relationship and be the sole provider of financial advice. ♦ It will generate a growing and recurring revenue stream. ♦ More control and flexibility over the fee structure.	♦ Appropriate for firms wanting to provide IA services without creating a separate entity because some of the CPAs can affiliate with another RIA or under a broker-dealer's RIA supervision. ♦ Education provided by the RIA or broker-dealer's RIA.	♦ Partnering is easy to establish. ♦ It requires only minimal capital resources. ♦ It does not require expertise in investment theory or vehicles, although the CPA must have a sufficient background to monitor the services.	♦ You have a smaller capital investment. ♦ You have a well-capitalized, experienced organization behind you. ♦ Education, performance reports, and marketing materials are typically provided by the broker-dealer. ♦ It enables CPAs to give investment advice to clients with minimal assets.
Cons	♦ It requires the greatest commitment of time and resources. ♦ The CPA must be knowledgeable about investment theory and advising, including asset allocation, risk tolerance, the full range of investment vehicles, and portfolio management, as well as regulatory and compliance rules. ♦ Higher practice set-up and maintenance costs because the CPA must maintain a "back office" to handle investment research, administrative, and compliance functions.	♦ The CPA must be knowledgeable about investment planning and products.	♦ The CPA gives the competitor direct access to the client and control over the client's financial decisions. ♦ The solicitor's agreement restricts the CPA's ability to provide certain types of investment advice and financial services. ♦ The CPA must ascertain if his or her state board of accountancy allows compensation in the form of commissions or referral fees from third parties.	♦ You and your staff will need additional licensing. ♦ The broker-dealer controls what you do, so you will have less flexibility. ♦ Clients may perceive a conflict of interest between the CPA's loyalty to the broker-dealer and the fiduciary responsibility to the client. ♦ CPA RRs who are not registered as IAs are limited in their advisory activities in that they may be prohibited from charging clients fees for advice. ♦ It may be difficult to adhere to the CPA's responsibilities, as outlined in the AICPA Code of Professional Conduct, given the conflicts that may arise. ♦ The CPA must ascertain if his or her state board of accountancy allows compensation in the form of commissions.
Compensation	RIA may charge fees based on a percentage of assets under management, on an hourly basis, or on a flat fee basis. RIA does not receive compensation contingent upon the purchase or sale of financial products.	IARs are typically compensated on a salary basis or a pro rata portion of the RIA's fee charged to clients.	Solicitors typically receive a referral fee based on a percentage of the RIA's or RR's management fee.	RRs receive compensation contingent upon the purchase or sale of financial products and also fees paid by the client. Fee-based advisers must generally be registered as an IA and RR.
Ongoing Compliance	♦ Form ADV amendment upon certain changes ♦ Annual updating amendment ♦ Disclosure to clients ♦ Bonding ♦ Limits on advisory fees ♦ Limits on advertising and certain business practices ♦ Restrictions on custody of client assets ♦ Avoiding conflict of interest situations ♦ Licensing of representatives ♦ Recordkeeping ♦ Capital or financial adequacy ♦ Drafting a code of ethics ♦ Compliance policies and procedures	♦ Examinations and qualifications ♦ Continuing education	♦ IA or IAR registration required in some states ♦ Furnish client with RIA's brochure, solicitor's brochure, and fee disclosure	♦ Form U-4 update upon changes ♦ Form U-5 upon termination ♦ Continuing education ♦ Duty of fair dealing to customers ♦ Suitability requirements for customers ♦ Restrictions on certain trading activities ♦ Restrictions on private securities transactions ♦ Restrictions on outside business activities ♦ Prohibition on conflicts of interest ♦ Disclosures to customers and broker-dealer

Appendix 2 - Resources

The CPA's Guide to Developing and Managing a PFP Practice

AICPA Code of Professional Conduct & Statement on Responsibilities in PFP Practice

Prudent Practices for Investment Advisors

AICPA PFP Practice Center

Information on:

- State Insurance Licensing Requirements
- State Investment Adviser Registration
- Investment Adviser Regulation
- Becoming a FINRA Member
- Broker-Dealer Regulation
- Qualifying Exams
- Investment Advisers Act of 1940

Appendix 3 - Definitions

Assets Under Management. Includes the securities portfolios for which the investment adviser provides continuous and regular supervisory or management services as of the date of filing Form ADV.[1]

Investment Adviser Registration Depository (IARD). An electronic filing system for Investment Advisers sponsored by the Securities and Exchange Commission and the North American Securities Administrators Association (NASAA), with FINRA serving as the developer and operator of the system. The IARD system collects and maintains the registration, reporting and disclosure information for Investment Advisers and their associated persons. The IARD system supports electronic filing of the revised Forms ADV and ADV-W, centralized fee and form processing, regulatory review, the annual registration renewal process, and public disclosure of Investment Adviser information.[2]

Investment Adviser. Any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities.[3]

Investment Adviser Representative. A supervised person of the investment adviser who has (i) more than five clients who are natural persons and (ii) more than ten percent of whose clients are natural persons. However, a supervised person is not an investment adviser representative if the supervised person (i) does not on a regular basis solicit, meet with, or otherwise communicate with clients of the investment adviser; or (ii) provides only impersonal investment advice.[4]

Person. A natural person or a company.[5]

Place of business. (1) an office at which the investment adviser representative regularly provides investment advisory services, solicits, meets with, or otherwise communicates with clients; and (2) any other location that is held out to the general public as a location at which the investment adviser representative provides investment advisory services, solicits, meets with or otherwise communicates with clients.[6]

Principal office and place of business. The executive office of the investment adviser from which the officers, partners, or managers of the investment adviser direct, control, and coordinate the activities of the investment adviser.[7]

Security. Any note, stock, treasury stock, security future, bond, debenture, evidence of indebtedness, certificate of interest, or participation in any profit sharing agreement; collateral-trust certificate, pre-organization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest

[1] Form ADV: Instruction for Part 1A, item 5.F.
[2] www.iard.com/WhatIsIARD.asp.
[3] Section 202(a)(11) of the Advisers Act, 15 U.S.C. §80b-2(a)(11).
[4] Advisers Act Rule 203A-3(a), 17 C.F.R. §275.203A-3(a)(1).
[5] Section 202(a)(16) of the Advisers Act.
[6] Advisers Act Rule 203A-3(b), 17 C.F.R. §275.203A-3(b).
[7] Advisers Act Rule 203A-3(c), 17 C.F.R. §275.203A-3(c).

in oil, gas, or other mineral rights; any put, call, straddle, option or privilege on any security (including a certificate of deposit) or on any group or index of securities (including any interest therein or based on the value thereof); or any put, call, straddle, option or privilege entered into a national securities exchange relating to foreign currency, or, in general, any interest or instrument commonly known as a "security," or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guaranty of, or warrant or right to subscribe to or purchase any of the foregoing.[8]

[8] Section 202(a)(18) of the Advisers Act, 15 U.S.C. §80b-2(a)(18).

Appendix 4 – SEC Release No. IA-1094

SECURITIES AND EXCHANGE COMMISSION Washington, D.C. 20549

[Rel. No. IA-1092]

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.

ACTION: Statement of staff interpretive position.

SUMMARY: The Commission is publishing the views of the staff of the Division of Investment Management on the applicability of the Investment Advisers Act of 1940 to financial planners and other persons who provide investment advice as a component of other financial services. The views expressed in this statement were developed jointly by Division staff and the North American Securities Administrators Association, Inc. ("NASAA") to update Investment Advisers Act Release No. 770 and provide uniform interpretations of the application of federal and state adviser laws to financial planners and other persons. The revised statement clarifies, among other things, the "business" element of the definition of investment adviser.

SUPPLEMENTARY INFORMATION: Since the Commission published Investment Advisers Act Rel. No. 770 (Aug. 13, 1981) ("IA-770"), the Commission and NASAA have worked together to promote more uniform regulation of investment advisers under federal and state securities laws. At the federal level, advisers are regulated under the Investment Advisers Act of 1940 ("Advisers Act"). Approximately 40 states regulate the activities of advisers under state adviser laws that typically are substantially similar to the Advisers Act. The staff of the Division and the NASAA Financial Planners/Investment Advisers Committee jointly developed the views stated in this release to provide uniform interpretations about the applicability of federal and state adviser laws to the activities of financial planners and other persons. While the views being published are based substantially on IA-770, this release revises IA-770 in some respects. Specifically, the revised release provides additional guidance on the fiduciary responsibilities of advisers, clarifies the "business" element of the definition of investment adviser, and supplements the views contained in IA-770 by references to interpretive letters issued by the Division since IA-770 was published.

I. BACKGROUND

Financial planning typically involves providing a variety of services, principally advisory in nature, to individuals or families regarding the management of their financial resources based upon an analysis of individual client needs. Generally, financial planning services involve preparing a financial program for a client based on the client's financial circumstances and objectives. This information normally would cover present and anticipated assets and liabilities, including insurance, savings, investments, and anticipated retirement or other employee benefits. The program developed for the client usually includes general recommendations for a course of activity, or specific actions, to be taken by the client. For example, recommendations may be made that the client obtain insurance or revise existing coverage, establish an individual retirement account, increase or decrease funds held in savings accounts, or invest funds in

securities. A financial planner may develop tax or estate plans for clients or refer clients to an accountant or attorney for these services.

The provider of such financial planning services in most cases assists the client in implementing the recommended program by, among other things, making specific recommendations to carry out the general recommendations of the program, or by selling the client insurance products, securities, or other investments. The financial planner may also review the client's program periodically and recommend revisions. Persons providing such financial planning services use various compensation arrangements. Some financial planners charge clients an overall fee for developing an individual client program while others charge clients an hourly fee. In some instances financial planners are compensated, in whole or in part, by commissions on the sale to the client of insurance products, interests in real estate, securities (such as common stocks, bonds, limited partnership interests, and mutual funds), or other investments.

A second common form of service relating to financial matters is provided by "pension consultants" who typically offer, in addition to administrative services, a variety of advisory services to employee benefit plans and their fiduciaries based upon an analysis of the needs of the plan. These advisory services may include advice as to the types of funding media available to provide plan benefits, general recommendations as to what portion of plan assets should be invested in various investment media, including securities, and, in some cases, recommendations regarding investment in specific securities or other investments. Pension consultants may also assist plan fiduciaries in determining plan investment objectives and policies and in designing funding media for the plan. They may also provide general or specific advice to plan fiduciaries as to the selection or retention of persons to manage the assets of the plan.[1] Persons providing these services to plans are customarily compensated for their services through fees paid by the plan, its sponsor, or other persons; by means of sales commissions on the sale of insurance products or investments to the plan; or through a combination of fees and commissions. Another form of financial advisory service is that provided by persons offering a variety of financially related services to entertainers or athletes based upon the needs of the individual client. Such persons, who often use the designation "sports representative" or "entertainment representative," offer a number of services to clients, including the negotiation of employment contracts and development of promotional opportunities for the client, as well as advisory services related to investments, tax planning, or budget and money management. Some persons providing these services to clients may assume discretion over all or a portion of a client's funds by collecting income, paying bills, and making investments for the client. Sports or entertainment representatives are customarily compensated for their services primarily through fees charged for negotiation of employment contracts but may also receive compensation in the form of fixed charges or hourly fees for other services provided, including investment advisory services.

There are other persons who, while not falling precisely into one of the foregoing categories, provide financial advisory services. As discussed below, financial planners, pension consultants,

[1] The authority to manage all or a portion of a plan's assets often is delegated to a person who qualifies as an "investment manager" under the Employee Retirement Income Security Act of 1974 [29 U.S.C. 1001 et seq.]. Under that statute, which is applicable to private sector pension and welfare benefit plans, an "investment manager" must be a registered investment adviser under the Advisers Act, a bank as defined in the Advisers Act, or an insurance company that is qualified to perform services as an investment manager under the laws of more than one state.

sports or entertainment representatives or other persons providing financial advisory services, may be investment advisers within the meaning of the Advisers Act, state adviser laws, or both.

II. STATUS AS AN INVESTMENT ADVISER

A. DEFINITION OF INVESTMENT ADVISER

Section 202(a)(11) of the Advisers Act defines the term "investment adviser" to mean:

> any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities.

Whether a person providing financially related services of the type discussed in this release is an investment adviser within the meaning of the Advisers Act depends upon all the relevant facts and circumstances. As a general matter, if the activities of any person providing integrated advisory services satisfy the elements of the definition, the person would be an investment adviser within the meaning of the Advisers Act, unless entitled to rely on one of the exclusions from the definition of investment adviser in clauses (A) to (F) of Section 202(a)(11).[2] A determination as to whether a person providing financial planning, pension consulting, or other integrated advisory services is an investment adviser will depend upon whether such person: (1) provides advice, or issues reports or analyses, regarding securities; (2) is in the business of providing such services; and (3) provides such services for compensation. These three elements are discussed below.

1. Advice or Analyses Concerning Securities

It would seem apparent that a person who gives advice or makes recommendations or issues reports or analyses with respect to specific securities is an investment adviser under Section 202(a)(11), assuming the other elements of the definition of investment adviser are met, *i.e.*, that such services are performed as a part of a business and for compensation. However, it has been asked on a number of occasions whether advice, recommendations, or reports that do not pertain to specific securities satisfy this element of the definition. The staff believes that a person who provides advice, or issues or promulgates reports or analyses, which concern securities, but which do not relate to specific securities, generally is an investment adviser under Section 202(a)(11), assuming the services are performed as part of a business[3] and for compensation. The staff has interpreted the definition of investment adviser to include persons who advise clients concerning the relative advantages and disadvantages of investing in securities in general as compared to other investments.[4] A person who, in the course of developing a financial program for a client, advises a client as to the desirability of investing in, purchasing or selling securities, as opposed to, or in relation to, any non-securities investment or financial vehicle would also be

[2] See discussion of Section 202(a)(11)(A) to (F) in Section IIB, *infra*.
[3] In this regard, as discussed in detail below, it is the staff's view that a person who gives advice or prepares analyses concerning securities generally may, nevertheless, not be "in the business" of doing so and, therefore, will not be considered an "investment adviser" as that term is used in Section 202(a)(11).
[4] *See, e.g., Richard K. May* (pub. avail. Dec. 11, 1979).

"advising" others within the meaning of Section 202(a)(11).[5] Similarly, a person who advises employee benefit plans on funding plan benefits by investing in, purchasing, or selling securities, as opposed to, or in addition to, insurance products, real estate not involving securities, or other funding media, would be "advising" others within the meaning of Section 202(a)(11). A person providing advice to a client as to the selection or retention of an investment manager or managers also, under certain circumstances, would be deemed to be "advising" others within the meaning of Section 202(a)(11).[6]

2. The "Business" Standard

Under section 202(a)(11), an investment adviser is one who, for compensation, (1) engages in the business of advising others as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or, alternatively, (2) issues or promulgates reports or analyses concerning securities as part of a regular business. Each of these two alternatives in the statutory definition of investment adviser contains a business test—one involves "engaging in the business" of advising others while the other involves issuing reports about securities as "part of a regular business." While the "business" standards established under Section 202(a)(11) are phrased somewhat differently, it is the staff's opinion that they should be interpreted in the same manner. In both cases, the determination to be made is whether the degree of the person's advisory activities constitutes being "in the business" of an investment adviser. The giving of advice need not constitute the principal business activity or any particular portion of the business activities of a person in order for the person to be an investment adviser under Section 202(a)(11). The giving of advice need only be done on such a basis that it constitutes a business activity occurring with some regularity. The frequency of the activity is a factor, but is not determinative.

Whether a person giving advice about securities for compensation would be "in the business" of doing so, depends upon all relevant facts and circumstances. The staff considers a person to be "in the business" of providing advice if the person: (i) holds himself out as an investment adviser or as one who provides investment advice, (ii) receives any separate or additional compensation that represents a clearly definable charge for providing advice about securities, regardless of whether the compensation is separate from or included within any overall compensation, or receives transaction based compensation if the client implements the investment advice, or (iii) on anything other than rare, isolated and non-periodic instances, provides specific investment

[5] See, e.g., *Thomas Beard* (pub. avail. May 8, 1975); *Sinclair-deMarinis Inc.* (pub. avail. May 1, 1981).

[6] *See, e.g., FPC Securities Corp.* (pub. avail. Dec. 1, 1974) (program to assist client in selection and retention of investment manager by, among other things, recommending investment managers to clients, monitoring and evaluating the performance of a client's investment manager, and advising client as to the retention of such manager); *William Bye Co.* (pub. avail. Apr. 26, 1973) (program involving recommendations to client as to selection and retention of investment manager based upon client's investment objectives and periodic monitoring and evaluation of investment manager's performance). On occasion in the past the staff has taken no-action positions with respect to certain situations involving persons providing advice to clients as to the selection or retention of investment managers. *See, e.g., Sebastian Associates, Ltd.*, (pub. avail. Aug. 7, 1975) (provision of assistance to clients in obtaining and coordinating the services of various professionals such as tax attorneys and investment advisers, including referring clients to such professionals, in connection with business as agent for clients with respect to negotiation of employment and promotional contracts); *Hudson Valley Planning Inc.* (pub. avail. Feb. 25, 1978) (provision of names of several investment managers to client upon request, without recommendation, in connection with business of providing administrative services to employee benefit plans.)

advice.[7] For the purposes of (iii) above, "specific investment advice" includes a recommendation, analysis or report about specific securities or specific categories of securities (e.g., industrial development bonds, mutual funds, or medical technology stocks). It includes a recommendation that a client allocate certain percentages of his assets to life insurance, high yielding bonds, and mutual funds or particular types of mutual funds such as growth stock funds or money market funds. However, specific investment advice does not include advice limited to a general recommendation to allocate assets in securities, life insurance, and tangible assets.

In applying the foregoing tests, the staff may consider other financial services activities offered to clients. For example, if a financial planner structures his planning so as to give only generic, non-specific investment advice as a financial planner, but then gives specific securities advice in his capacity as a registered representative of a dealer or as agent of an insurance company, the person would not be able to assert that he was not "in the business" of giving investment advice. See discussion of the broker-dealer exception set forth in Section 202(a)(11)(C) of the Advisers Act, infra. In the staff's view, it is necessary to consider these other financial services activities. Section 208(d) of the Advisers Act makes it illegal for someone to do indirectly under the Advisers Act what cannot be done directly.

3. Compensation

The definition of investment adviser applies to persons who give investment advice for compensation. This compensation element is satisfied by the receipt of any economic benefit, whether in the form of an advisory fee or some other fee relating to the total services rendered, commissions, or some combination of the foregoing. It is not necessary that a person who provides investment advisory and other services to a client charge a separate fee for the investment advisory portion of the total services. The compensation element is satisfied if a single fee is charged for a number of different services, including investment advice or the issuing of reports or analyses concerning securities within the meaning of the Advisers Acts.[8] As discussed above, however, the fact that no separate fee is charged for the investment advisory portion of the service could be relevant to whether the person is "in the business" of giving investment advice.

It is not necessary that an adviser's compensation be paid directly by the person receiving investment advisory services, only that the investment adviser receive compensation from some source for his services.[9] Accordingly, a person providing a variety of services to a client, including investment advisory services, for which the person receives any economic benefit, for example, by receipt of a single fee or commissions upon the sale to the client of insurance products or investments, would be performing such advisory services "for compensation" within the meaning of Section 202(a)(11) of the Advisers Act.[10]

B. EXCLUSIONS FROM DEFINITION OF INVESTMENT ADVISER

[7] *See Zinn v. Parish*, 644 F.2d 360 (7th Cir. 1981).
[8] *See, e.g., FINESCO* (pub. avail. Dec. 11, 1979).
[9] *See, e.g., Warren H. Livingston* (pub. avail. Mar. 8, 1980).
[10] Section 202(a)(11)(C) of the Advisers Act excludes from the definition of investment adviser a broker or dealer who performs investment advisory services that are incidental to the conduct of its broker or dealer business and who receives no special compensation therefor. *See* discussion of Section 202(a)(11)(C), *infra*.

Clauses (A) to (E) of Section 202(a)(11) of the Advisers Act set forth limited exclusions from the definition of investment adviser available to certain persons.[11] Whether an exclusion from the definition of investment adviser is available to any financial planner, pension consultant or other person providing investment advisory services within the meaning of Section 202(a)(11), depends upon the relevant facts and circumstances.

A person relying on an exclusion from the definition of investment adviser must meet all of the requirements of the exclusion. The staff's view is that the exclusion contained in Section 202(a)(11)(B) is not available, for example, to a lawyer or accountant who holds himself out to the public as providing financial planning, pension consulting, or other financial advisory services. In such a case it would appear that the performance of investment advisory services by the person would not be incidental to his practice as a lawyer or accountant.[12] Similarly, the exclusion for brokers or dealers contained in Section 202(a)(11)(C) would not be available to a broker or dealer, or associated person of a broker or dealer, acting within the scope of the business of a broker or dealer, if the person receives any special compensation for providing investment advisory services.[13] Moreover, the exclusion from the definition of investment adviser contained in Section 202(a)(11)(C) is only available to an associated person of a broker or dealer or "registered representative" who provides investment advisory services to clients within the scope of the person's employment with the broker or dealer.[14] For example, if a registered representative provides advice independent of, or separate from, his broker or dealer employer such as by establishing a separate financial planning practice, then he could not rely on the exclusion because his investment advisory activities would not be subject to control by his

[11] Section 202(a)(11) provides that the definition of investment adviser does not include:

(A) a bank, or any bank holding company as defined in the Bank Holding Company Act of 1956, which is not an investment company;

(B) any lawyer, accountant, engineer or teacher whose performance of such [advisory] services is solely incidental to the practice of his profession;

(C) any broker or dealer whose performance of such [advisory] services is solely incidental to the conduct of his business as a broker or dealer and who receives no special compensation therefor;

(D) the publisher of any bona fide newspaper, news magazine or business or financial publication of general and regular circulation;

(E) any person whose advice, analyses, or reports related to no securities other than securities which are direct obligations of or obligations guaranteed as to principal or interest by the United States, or securities issued or guaranteed by corporations in which the United States has a direct or indirect interest which shall be designated by the Secretary of the Treasury, pursuant to Section 3(a)(12) of the Securities Exchange Act of 1934, as exempted securities for the purposes of that Act.

Section 202(a)(11)(F) excludes from the definition of investment adviser "such other persons not within the intent of this paragraph, as the Commission may designate by rules and regulations or order."

[12] *See, e.g., Mortimer M. Lerner* (pub. avail. Feb. 15, 1980); *David R. Markley* (pub. avail. Feb. 8, 1985); *Hauk, Soule & Fasani, P.C.* (pub. avail. May 1, 1986). The "professional" exclusion provided in Section 202(a)(11)(B) by its terms is only available to lawyers, accountants, engineers, and teachers. A person engaged in a profession other than one of those enumerated in Section 202(a)(11)(B) who performs investment advisory services would be an investment adviser within the meaning of Section 202(a)(11) whether or not the performance of investment advisory services is incidental to the practice of such profession. Unless another basis for excluding the person from the definition of investment adviser is available, the person would be subject to the Advisers Act.

[13] *See, e.g., FINESCO, supra* note 8. For a general statement of the views of the staff regarding special compensation under Section 202(a)(11)(C), *see* Investment Advisers Act Release No. 640 (October 5, 1978), and *Robert S. Strevell* (pub. avail. April 29, 1985). *See* discussion of the "business" standard, *supra.*

[14] *See, e.g., Corinne E. Wood* (pub. avail. April 17, 1986); *George E. Bates* (pub. avail. April 26, 1979).

broker or dealer employer.[15] Similarly, the exclusion would be unavailable if he provides advice without the knowledge and approval of his employer because in that capacity his advisory activities would, by definition, be outside the control of his employer.[16]

III. REGISTRATION AS AN INVESTMENT ADVISER

Any person who is an investment adviser within the meaning of Section 202(a)(11) of the Advisers Act, who is not excluded from the definition of investment adviser by virtue of one of the exclusions in Section 202(a)(11), and who makes use of the mails or any instrumentality of interstate commerce in connection with the person's business as an investment adviser, is required by Section 203(a) of the Advisers Act to register with the Commission as an investment adviser unless specifically exempted from registration by Section 203(b) of the Advisers Act.[17] Also, any person who is an investment adviser within the meaning of any state investment adviser definition, and who is not excluded from that definition, may be required to register with that state. The materials necessary for registering with the Commission as an investment adviser can be obtained by writing the Publications Unit, Securities and Exchange Commission, Washington, D.C., 20549. As to the various states, persons should contact the office of the state securities administrator in the state in which they must register to obtain the necessary materials.

IV. APPLICATION OF ANTIFRAUD PROVISIONS

The antifraud provisions of Section 206 of the Advisers Act [15 U.S.C. 80b-6], and the rules adopted by the Commission thereunder, apply to any person who is an investment adviser as defined in the Advisers Act, whether or not the person is required to be registered with the Commission as an investment adviser.[18] Sections 206(1) and (2) of the Advisers Act, upon which many state antifraud provisions are patterned, make it unlawful for an investment adviser, directly or any indirectly, to "employ any device, scheme, or artifice to defraud client or prospective client" or to "engage in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client."[19] An investment adviser is a

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[15] *See, e.g., Robert S. Strevell*, *supra* note 13; *Elmer D. Robinson* (pub. avail. Jan. 6, 1986); *Brent A. Neiser* (pub. avail. Jan. 21, 1986).

[16] *Id.*

[17] Section 203(b) exempts from registration:

(1) any investment adviser all of whose clients are residents of the State within which such investment adviser maintains his or its principal office and place of business, and who does not furnish advice or issue analyses or reports with respect to securities listed or admitted to unlisted trading privileges on any national securities exchange;
(2) any investment adviser whose only clients are insurance companies; or
(3) any investment adviser who during the course of the preceding twelve months has had fewer than fifteen clients and who neither holds himself out generally to the public as an investment adviser nor acts as an investment adviser to any investment company registered under the [Investment Company Act].

[18] The antifraud provisions of some state statutes may apply to any person receiving consideration from another person for rendering investment advice even if the person rendering the investment advice is technically excluded from the state definition of investment adviser.

[19] In addition, Section 206(3) of the Advisers Act generally makes it unlawful for an investment adviser acting as principal for his own account knowingly to sell any security to or purchase any security from a client, or, acting as broker for a person other than such client, knowingly to effect any sale or purchase of any security for the account of such client, without disclosing to such client in writing before the completion of such transaction the capacity in which he is acting and obtaining the consent of the client to such transaction. The responsibilities of an investment

fiduciary who owes his clients "an affirmative duty of 'utmost good faith, and full and fair' disclosure of all material facts."[20] The Supreme Court has stated that a "failure to disclose material facts must be deemed fraud or deceit within its intended meaning, for, as the experience of the 1920's and 1930's amply reveals, the darkness and ignorance of commercial secrecy are the conditions under which predatory practices best thrive."[21] Accordingly, the duty of an investment adviser to refrain from fraudulent conduct includes an obligation to disclose material facts to his clients whenever the failure to do so would defraud or operate as a fraud or deceit upon any client or prospective client. In this connection the adviser's duty to disclose material facts is particularly pertinent whenever the adviser is in a situation involving a conflict, or potential conflict, of interest with a client.

The type of disclosure required by an investment adviser who has a potential conflict of interest with a client will depend upon all the facts and circumstances. As a general matter, an adviser must disclose to clients all material facts regarding the 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. The following examples, which have been selected from cases and staff interpretive and no-action letters, illustrate the scope of the duty to disclose material information to clients in certain common situations involving conflicts of interests.

The advisers' duty to disclose material facts includes the duty to disclose the various capacities in which he might act when dealing with any particular client. For example, an adviser who intends to implement the financial plans he prepares for clients, in whole or part, through the broker or dealer or insurance company with whom the adviser is associated, should inform a client that in implementing the plan the adviser will also act as agent for the broker or dealer or the insurance company.[22]

An investment adviser who is also a registered representative of a broker or dealer and provides investment advisory services outside the scope of his employment with the broker or dealer must disclose to his advisory clients that his advisory activities are independent from his employment with the broker or dealer.[23] Additional disclosures would be required, depending on the circumstances, if the investment adviser recommends that his clients execute securities transactions through the broker or dealer with which the investment adviser is associated. For example, the investment adviser would be required to disclose fully the nature and extent of any interest the investment adviser has in such recommendation, including any compensation the investment adviser would receive from his employer in connection with the transaction.[24] In

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adviser dealing with a client as principal or as agent for another person are discussed in Advisers Act Rel. Nos. 40 and 470 (February 5, 1945 and August 20, 1975 respectively).

[20] *SEC v. Capital Gains Research Bureau*, 375 U.S. 180, 184 (1963) quoting Prosser, *Law of Torts* (1955), 534-535.

[21] *Id.* at 200.

[22] *See Elmer D. Robinson*, *supra* note 15. *See also In the Matter of Haight & Co., Inc.* (Securities Exchange Act Rel. No. 9082, Feb. 19, 1971), where the Commission held that a broker or dealer and its associated persons defrauded its customers in the offer and sale of securities by holding themselves out as financial planners who would, as financial planners, give comprehensive and expert planning advice and choose the best investments for their clients from all available securities, when in fact they were not expert in planning and made their decisions based on the receipt of commissions and upon their inventory of securities. *Accord Institutional Trading Corporation* (pub. avail. Nov. 27, 1972).

[23] *David P. Atkinson* (pub. avail. Aug. 1, 1977). *See also Corrine E. Wood*, *supra* note 14.

[24] *Id.*

addition, the investment adviser would be required to inform his clients of their ability to execute recommended transactions through other brokers or dealers.[25] A financial planner who will recommend or use only the financial products offered by his broker or dealer employer when implementing financial plans for clients should disclose this practice to clients[26] and inform clients that the plan may be limited by the products offered by the broker or dealer. Finally, the Commission has stated that "an investment adviser must not effect transactions in which he has a personal interest in a manner that could result in preferring his own interest to that of his advisory clients."[27]

An investment adviser who structures his personal securities transactions to trade on the market impact caused by his recommendations to clients must disclose this practice to clients.[28] An investment adviser generally also must disclose if his personal securities transactions are inconsistent with the advice given to clients.[29] Finally, an investment adviser must disclose compensation received from the issuer of a security being recommended.[30]

Unlike other general antifraud provisions in the federal securities laws which apply to conduct "in the offer or sale of any securities"[31] or "in connection with the purchase or sale of any security,"[32] the pertinent provisions of Section 206 do not refer to dealings in securities but are stated in terms of the effect or potential effect of prohibited conduct on the client. Specifically, Section 206(1) prohibits "any device, scheme, or artifice to defraud any client or prospective client," and Section 206(2) prohibits "any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client." In this regard, the Commission has applied Sections 206(1) and (2) in circumstances in which the fraudulent conduct arose out of the investment advisory relationship between an investment adviser and its clients, even though the conduct does not involve a securities transaction. For example, in an administrative proceeding brought by the Commission against an investment adviser, the respondent consented to a finding by the Commission that the respondent had violated Sections 206(1) and (2) by persuading its clients to guarantee its bank loans and ultimately to post their securities as collateral for its loans without disclosing the adviser's deteriorating financial condition, negative net worth, and other outstanding loans.[33] Moreover, the staff has taken the position that an investment adviser who sells non-securities investments to clients must, under Sections 206(1) and (2), disclose to clients and prospective clients all its interests in the sale to them of such non-securities investments.[34]

V. NEED FOR INTERPRETIVE ADVICE

[25] *Don P. Matheson* (pub. avail. Sept. 1, 1976).
[26] *Elmer D. Robinson, supra* note 15.
[27] *Kidder, Peabody & Co., Inc.,* 43 S.E.C. 911,916 (1968).
[28] *SEC v. Capital Gains Research Bureau, supra* note 19, at 197.
[29] *In the Matter of Dow Theory Letters et al.*, Advisers Act Rel. No. 571 (Feb. 22, 1977).
[30] *In the Matter of Investment Controlled Research et al.*, Advisers Act Release No. 701 (Sept. 17, 1979).
[31] Section l7(a) [15 U.S.C. 77q(a)] of the Securities Act of 1933 [15 US.C. 77a *et seq*.].
[32] Rule l0b-5 [17 CFR 240.l0b-5] under the Securities Exchange Act of 1934 [15 U.S.C. 78a *et seq*.]. *See also* Section 15 (c) [15 U.S.C. 78o(c)] of the Securities Exchange Act of 1934.
[33] *In the Matter of Ronald B. Donati, Inc. et al.*, Advisers Act Rel. Nos. 666 and 683 (February 8, 1979 and July 2, 1979 respectively). *See also Intersearch Technology, Inc.* [1974-1975 Transfer Binder] Fed. Sec. L. Rep. (CCH) Paragraph 80,139, at 85,189.
[34] *See Boston Advisory Group* (pub. avail. Dec. 5, 1976).

The general interpretive guidance provided in this release should facilitate greater compliance with the Advisers Act and the investment adviser laws of the states. The staff of the Commission will respond to routine requests for no-action or interpretive advice relating to the status of persons engaged in the types of businesses described in this release by referring persons making the requests to the release, unless the requests present novel factual or interpretive issues such as material departures from the nature and type of services and compensation arrangements discussed above. Requests for no-action or interpretive advice from the staff of the Commission should be submitted in accordance with the procedures set forth in Investment Advisers Act Release No. 281 (Jan. 25, 1971). As to requests for no-action or interpretive advice from the states, persons should contact the various state securities departments to inquire as to their procedures.

Accordingly, Part 276 of Chapter 11 of Title 17 of the Code of Federal Regulations is amended by adding Investment Advisers Act Release No. IA-1092, Statement of the staff as to the 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, which supersedes IA-770.

By the Commission.

Jonathan G. Katz, Secretary

DATE: October 8, 1987

Appendix 5 – Descriptions For CPA And PFS – Part 2B Of Form ADV

Descriptions for CPA and PFS—Part 2B of Form ADV (*Brochure Supplement)*

Amendments[1] to Part 2B of Form ADV require advisers to prepare narrative brochures written in plain English which contain, among other things, information on the educational and business background of management and key advisory personnel of the adviser[2]. The SEC permits, *but does not require*, advisers to list the professional designations held by such persons. SEC instructions require, however, that any listing of professional designations held *must* provide a sufficient explanation of the minimum qualifications required for the designation to allow clients and potential clients to understand the value of the designation.

Certified Public Accountant (CPA)[3] CPAs are licensed and regulated by their state boards of accountancy. While state laws and regulations vary, the education, experience and testing requirements for licensure as a CPA generally include minimum college education (typically 150 credit hours with at least a baccalaureate degree and a concentration in accounting), minimum experience levels (most states require at least one year of experience providing services that involve the use of accounting, attest, compilation, management advisory, financial advisory, tax or consulting skills, all of which must be achieved under the supervision of or verification by a CPA), and successful passage of the Uniform CPA Examination. In order to maintain a CPA license, states generally require the completion of 40 hours of continuing professional education (CPE) each year (or 80 hours over a two-year period or 120 hours over a three-year period). Additionally, all American Institute of Certified Public Accountants (AICPA) members[4] are required to follow a rigorous *Code of Professional Conduct*, which requires that they act with integrity, objectivity, due care, competence, fully disclose any conflicts of interest (and obtain client consent if a conflict exists), maintain client confidentiality, disclose to the client any commission or referral fees, and serve the public interest when providing financial services. The vast majority of state boards of accountancy have adopted the AICPA's *Code of Professional Conduct* within their state accountancy laws or have created their own.

Personal Financial Specialist (PFS)[5] The PFS credential demonstrates that an individual has met the minimum education, experience, and testing required of a CPA in addition to a minimum level of expertise in personal financial planning. To attain the PFS credential, a candidate must hold a valid and unrevoked CPA license, permit or certificate issued by a legally constituted state authority, fulfill 3,000 hours of personal financial planning business experience, complete 75 hours of personal financial planning CPE credits, pass a comprehensive financial planning exam and be an active member of the AICPA. A PFS credential holder is required to adhere to AICPA's *Code of Professional Conduct*, and is encouraged to follow AICPA's *Statement on Responsibilities in Personal Financial Planning*

[1] See "Amendments to Form ADV," IA Release No. 3060 (July 28, 2010).
[2] Form ADV Part 2B, Item 2, *Educational Background and Business Experience*.
[3] This description represents the requirements as of 1/1/2013. It is the responsibility of the adviser to disclose the qualifications in place when he or she attained the license.
[4] As well as any non-AICPA members whose state board of accountancy has adopted either the AICPA *Code of Professional Conduct* or a similar ethical code.
[5] This description represents the requirements as of 1/1/2013. It is the responsibility of the adviser to disclose the qualifications in place when he or she attained the credential.

Practice. To maintain their PFS credential, the recipient must complete 60 hours of financial planning CPE credits every three years. The PFS credential is administered through the AICPA.

Note: These descriptions are provided by the AICPA as guidance to its members who choose to list their professional designations on Part 2B of Form ADV, the uniform form used by investment advisers to register with the Securities and Exchange Commission (SEC). Listing the CPA license and/or the PFS credential and the descriptions thereof is optional and is solely at the discretion of the individual licensee and/or credential holder. This language has neither been reviewed nor approved by the SEC, state boards of accountancy or other third parties. It is the responsibility of the adviser to comply with all applicable laws and regulations and to obtain counsel from their legal counsel and/or compliance advisor in determining whether to list their license and/or credential on Form ADV, including whether to use the language provided by AICPA.

Appendix 6 – Form ADV

A PDF of Form ADV (Part 1 and Part 2) can be found at the SEC's website:

www.sec.gov/about/forms/formadv.pdf

Further information on "Electronic Filing for Investment Advisers" can be found at:

www.sec.gov/divisions/investment/iard/iastuff.shtml

and

www.iard.com

