JACKSON, GRANT
INVESTMENT ADVISERS, INC.

JULIE JASON, PRESIDENT
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July 25, 2009

Elizabeth M. Murphy, Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington D.C. 20549-1090

RE: Custody of Funds or Securities by Clients of Investment Advisers
File No. S7-09-09

Dear Secretary Murphy:

This letter is in response to the Commission's request for comment[1] on its proposal to provide "additional safeguards under the Advisers Act when an adviser has custody of client funds or securities."

We are registered investment advisers who, like the overwhelming majority (82 percent) of SEC registered advisers, are small firms with 10 or fewer employees[2]. Like most registered investment advisers, our firm does not hold client funds or securities. Instead, our client's funds and securities are held by an independent "qualified custodian" that is subject to "extensive regulation and oversight." Our clients receive statements directly from the custodian that show all funds, securities and activity in their accounts. The custodian is subject to stringent auditing requirements under current law. We are subject to surprise audits by the SEC; such audits already include custody of client funds and securities.

[1]Custody of Funds or Securities of Clients by Investment Advisers-File No. S7-09-09; SEC Release No. IA-2876; 34-57419 Dated May 27, 2009
[2] Of the 10,817 advisers registered with the Commission as of September 30, 2007, 8,835 have 10 or fewer employees. Only 1,952 advisers have 11 to 999 employees (medium size advisers) and only 30 advisers have 1,000 or more employees (large advisers).

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While the Commission's proposal focuses on providing "additional safeguards under the Advisers Act when an adviser has custody of client funds or securities," it actually reaches far beyond that objective to those advisers such as our firm, who do NOT custody client assets.

Under the proposal, our firm would be required to retain an independent CPA at our expense to perform annual or more frequent surprise audits of client assets even though we do not custody client assets. We strongly oppose this proposal as unnecessary, burdensome, and beyond the Commission's stated goals.

A casual reader might be confused at this point. If the Commission's goal is to provide safeguards when an adviser has custody, why does the proposal extend to advisers who don't have custody? It turns out that even in situations in which advisers do not hold client assets, the Commission deems the adviser to be a custodian if the adviser has the authority to deduct advisory fees from client accounts, as we and the vast majority of advisers do.[3]

The Commission has asked for comment on whether this type of non-custodial, fee deducting adviser should be exempt from the proposed surprise examination requirement.

The answer is a resounding "yes." Advisers who are deemed custodians solely by reason of fee deduction authority[4] should be exempted because current regulatory oversight is effective as to those advisers. Such advisers are already audited by the Commission. The direct delivery of statements by the independent custodian deters unscrupulous advisers from fraudulent activities[5]. No additional advantages will be gained through outside CPA surprise audits.

Moreover, there are practical reasons for our position.

[3] According to rule 206(4)-2 as revised in 2003, the adviser is the custodian if the adviser charges a fee for services that is deducted from clients' accounts.
[4] Note that the Commission recognizes that non-custodial fee-deducting advisers are not custodians for purposes of ADV disclosure requirements[4]. Instructions to the ADV tell non-custodial fee-authority advisers to view themselves as non-custodial for purposes of the ADV.
[5] Custody of Funds or Securities of Clients by Investment Advisers, Release No.cIA-2176 (September 25, 2003, 68 Fed. Reg. 56692, 56693 (October 1, 2003).

First, the custodian prepares monthly statements showing client funds and securities and provides them to us and to our clients. If, on an audit, we were asked to provide information about customer funds and securities, we would provide the statements issued by the independent custodian – that's the official record of what is held in a client's account. Unless you control the custodian, there is no way to influence what is reported on that official record prepared independently by the custodian.

Second, even if we were asked for this information on a surprise basis, we would still provide custodian statements. The element of surprise would not alter the information provided.

Third, surprise audits are disruptive. The adviser has to cancel scheduled meetings and activities when the auditors arrive at the place of business. There is no advance warning. There is no opportunity to call appointments to reschedule them. As a result, the offsetting regulatory benefits of initiating additional surprise audits would need to be clearly quantifiable and justified to offset the burden on the adviser.

Fourth, if the goal is to avoid future Ponzi schemes, the focus on non-custodial advisers is misplaced. A light should be shined on custodial advisers, such as Madoff. Even better would be a universal requirement that all advisers custody client assets solely with independent custodians.

Fifth, after Sarbanes-Oxley, independent CPAs have increased the costs of their audits. The cost of an outside audit would have to be borne by the adviser. Some firms would have to reduce staff or raise fees to cover these costs, neither of which is a benefit to clients.

Sixth, we do not believe the proposal to perform surprise CPA audits of non-custodian fee-deducting advisers will advance the Commission's stated goal of providing "additional safeguards under the Advisers Act when an adviser has custody of client funds or securities."

The reality is that this type of custodian simply does not have custody of client funds or securities.

We recognize that the Commission has been pilloried for failure to uncover Bernie Madoff's massive Ponzi scheme. Madoff was a registered investment adviser whose clients' funds and securities were not held by an independent custodian. We recognize the Commission's need to tighten its regulatory regime to attempt to prevent such failures. As such, we understand the rationale behind the Commission's proposing changes to rule 206(4)-2 under the Advisers Act, is to "improve the safekeeping of client assets."

While we applaud the Commission for this regulatory initiative as it applies to advisers who do control custody, it should not extend to non-custodial advisers merely because they have billing authority.

What can the Commission do to improve safekeeping? Require all advisers to custody client assets with an independent custodian as we do. Independent custody makes the fraudster's agenda virtually impossible to accomplish.

Respectfully Submitted

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