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July 28, 2009

VIA ELECTRONIC DELIVERY

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

Re: Investment Advisers Act Release No. 2876 (File No. S7-09-09): Custody of Funds or Securities of Clients by Investment Advisers

Dear Ms. Murphy:

We respectfully submit this letter in response to a request by the Securities and Exchange Commission ("SEC" or "Commission") for comments regarding the proposed amendments ("Proposed Amendments" or "Proposed Custody Rule") to Rule 206(4)-2 ("Custody Rule" or "Rule") under the Investment Advisers Act of 1940, as amended ("Advisers Act") relating to custody of funds or securities of clients by registered investment advisers.[1]

Dechert LLP is an international law firm with a wide-ranging financial services practice that serves clients in the United States and worldwide. Our clients include U.S. based and non-U.S. based investment advisers, private funds, private funds of funds and private equity funds as well as fund administrators, broker-dealers, pension plans, insurance companies, commercial and investment banks and thrift institutions. Thus, our clients include registered investment advisers who are subject to the Custody Rule, persons who invest (either on their own behalf or in a fiduciary capacity) with or through such advisers, and custodians. Our services for these clients include assistance with respect to

[1] *See Custody of Funds or Securities of Clients by Investment Advisers*, Rel. No. IA-2876 (May 20, 2009) ("*2009 Release*").

compliance with the federal securities laws. In developing these comments, we have drawn on our extensive experience in the investment management industry. Although we have discussed the matters addressed in the Proposed Amendments with some of our clients, the comments that follow reflect our own views and not necessarily those of any client of the firm.

The Commission proposes to extend to virtually all registered investment advisers with custody of client funds and securities the requirement that an independent public accountant conduct an annual surprise examination to verify the funds and securities in a client's account ("Surprise Examination").[2] The Proposed Custody Rule would eliminate the current exception from Surprise Examinations that is available to (i) advisers that cause custodians to deliver quarterly account statements to their clients, and (ii) limited partnerships, limited liability companies or other types of privately placed pooled investment vehicles ("private funds") that comply with the requirement to deliver to investors, on an annual basis, audited financial statements prepared in compliance with U.S. generally accepted accounting principles ("GAAP"). In this regard, the Commission has stated that a Surprise Examination "would provide 'another set of eyes' on client assets, and thus additional protection against their misuse."[3]

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2 The purpose of the Surprise Examination is to verify the continued existence and safekeeping of assets and to assure that assets have not been misappropriated by the adviser. Consequently, the independent public accountant performing the Surprise Examination:

> generally must: (i) confirm with the custodian *all* cash and securities held by the custodian, including physical examination of securities if applicable, and will [*sic*] reconcile all such cash and securities to the books and records of client accounts maintained by the adviser; (ii) verify the books and records of client accounts maintained by the adviser by examining the securities records and transactions since the last examination and by confirming with clients *all* funds and securities in client accounts; and (iii) confirm with clients, on a test basis, closed accounts or securities or funds that have been returned since the last examination.

2009 Release, *supra* note 1, at n. 8 and accompanying text. The Surprise Examination must conform to U.S. Generally Accepted Auditing or Attestation Standards and any other requirements imposed by the SEC, except that all client funds and securities covered by the Surprise Examination must be actually verified or substantiated (*i.e.*, no sampling is permitted). *Id.* Finally, the independent accountant must include "any other audit procedures it deems necessary under the circumstances." *Id.* at n. 45.

3 *2009 Release*, *supra* note 1, at text following n. 16.

While we support the Commission's goals of investor protection and accountability for investment advisers, we believe that the Proposed Custody Rule will impose unnecessary costs and burdens upon the vast majority of investment advisers that are subject to the Custody Rule. In addition, we believe that less burdensome and expensive alternatives exist that would protect clients of investment advisers (and investors in those clients). In particular, we are concerned that requiring Surprise Examinations for an adviser that is deemed to have custody of client assets solely as a result of certain billing arrangements with its clients is unnecessary. Similarly, requiring Surprise Examinations for an adviser that is deemed to have custody of a private fund's assets solely because it or its affiliate serves as general partner or managing member to the private fund would increase costs to investors without providing them with the benefits the Commission desires.

Pursuant to the Commission's request for comments, we offer the following analysis of these and other interpretive and implementation issues raised by the Proposed Amendments, along with suggestions for improvements to the regulation of covered entities. Our specific suggestions are as follows:

- Advisers should no longer be deemed to have custody solely as a result of automatic debiting of advisory fees.
- The Custody Rule should not require the use of an independent custodian. However, the use of an independent custodian should be a requirement for advisers seeking to rely on certain exceptions from the Rule (*e.g.*, if the Commission continues to define custody to include automatic debiting of advisory fees, advisers who use an independent custodian should be excepted from the Surprise Examination requirement).
- The Commission should clarify the continued applicability of certain staff positions, including relevant interpretations and no-action positions included in the staff's FAQ regarding the Custody Rule,[4] in any adopting release and/or codify into the Custody Rule certain of those staff positions.
- The Commission should clarify that the Custody Rule does not require advisers to send account statements to clients, separate and apart from those that would be required to be sent by the qualified custodian.

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[4] See *Staff Responses to Questions about Amended Custody Rule, available at* http://www.sec.gov/divisions/investment/custody_faq.htm (modified Jan. 10, 2005) ("*Custody FAQ*").

- Custody by an affiliate should not, in and of itself, cause an adviser to be deemed to have custody. Rather, the Commission should make this a rebuttable presumption and set forth factors or a mechanism for rebutting the presumption. In particular, a non-discretionary account custodied at an affiliated qualified custodian should not cause a non-discretionary adviser to be deemed to have custody of such an account.
- The Commission should provide a reasonable transition period of at least 18 months prior to the effectiveness of the internal control report requirement.
- Advisers to private funds should have an alternate means to comply with the Custody Rule, which does not include a Surprise Examination Requirement, where such means (discussed below) provide equivalent protection to investors.
- For advisers to private funds that choose to rely on the Account Statement Method (as defined below), delivery of account statements by an independent administrator (rather than the qualified custodian) should be sufficient.
- For advisers to private funds that choose to rely on the Audit Method (as defined below), a mechanism for relief should be provided where, for reasons beyond the adviser's control, the audit: (i) cannot be delivered timely; or (ii) deviates from GAAP in an immaterial manner.
- The Commission should set reasonable bounds on the scope of the Surprise Examination for private funds, including, for example, that the accountant should be required only to verify the existence and safekeeping of client assets. The Commission explicitly should affirm that the Surprise Examination does not require an accountant to review the adviser's valuation of privately offered securities.
- The Commission should impose different requirements for account statements provided to private fund investors when an adviser to a private fund relies on the Account Statement Method, as the requirements currently imposed by the Custody Rule would result, in many cases, in quarterly statements that are of questionable utility and confusing for most private fund investors.
- The Commission should restore the staggered 120-day/180-day deadlines under the Audit Method for private funds and private funds of funds, respectively.

Each of these recommendations is described in greater detail below.

APPLICATION TO ALL ADVISERS

Surprise Examinations of advisers who are deemed to have custody solely as a result of fee billing practices would impose undue burdens on these advisers that are not commensurate with the protections that might be afforded by annual Surprise Examinations of these advisers

We believe that the vast majority of advisers who are subject to the Custody Rule are deemed to have custody only as a result of automatic debiting of advisory fees from advisory accounts. Many clients and advisers prefer the certainty and convenience of these arrangements. For clients, automatic debiting of advisory fees from advisory accounts provides several benefits. It reduces the amount of paperwork associated with the account and allows for a better picture of the account's performance, because advisory fees are reflected in cash flows. For advisers, automatic debiting of advisory fees provides other benefits. It assures that payment will be timely and avoids the need to separately bill clients or deal with the potential need to collect from clients who forget (or refuse) to pay the amount owed for services rendered. While we understand that these arrangements provide the theoretical ability for an adviser to withdraw amounts in excess of the agreed-upon fee, we do not believe that these arrangements have been (or are likely to be) subject to significant fraudulent activities or abuses,[5] given the various regulatory and business practice safeguards already in place.[6]

Nevertheless, the Proposed Amendments would subject all advisers who are deemed to have "custody" to an annual Surprise Examination. However, the direct and indirect costs of requiring annual Surprise Examinations do not appear to be commensurate with

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[5] In fact, we are unaware of any published case or settled enforcement action where an adviser was found to have used fee billing authority (as opposed to other means of accessing a client's assets) to misappropriate funds from a client's account. We are aware of a recently filed enforcement action in which an adviser was alleged to have used the fee deduction power to withdraw fees well in excess of amounts owed. *See SEC Obtains Emergency Relief to Halt Fraud Conducted by Omaha, Nebraska Investment Adviser*, Lit. Rel. No. 21113 (July 1, 2009) (announcing the commencement of enforcement proceedings in *SEC v. Ryan M. Jindra and Envision Investment Advisors, LLC* Case n. 8:09-CV-00216-JFB-TDT (D. Neb.)).

[6] In addition to the delivery of quarterly account statements and other regulatory protections, we understand that many custodians (including most that are likely to have custody over client assets that are subject to direct billing relationships) place limits on the amount of assets that can be withdrawn by an adviser in connection with an automatic fee arrangement.

any benefits that might be achieved. The Commission's cost/benefit analysis assumes that the cost of a Surprise Examination will be approximately $8,100 per adviser.[7] We believe that this amount significantly underestimates the cost of an annual Surprise Examination and does not consider the loss of convenience that would result from advisers abandoning automatic billing in order to avoid annual Surprise Examinations. Currently, we understand that: (i) some of our clients pay upwards of triple that amount when engaging a mid-size audit firm to perform a Surprise Examination; and (ii) the amount paid is based, in part, on the number of accounts. Moreover, as discussed below, advisers to private funds of funds and private equity funds may be disproportionally impacted, as Surprise Examinations for such private funds are likely to be among the more costly and many of these firms are smaller and comparatively less well capitalized. Under the current Custody Rule, only those accounts for which quarterly statements are not delivered by a qualified custodian are subject to the Surprise Examination requirement. Under the Proposed Amendments, all accounts for which advisers have custody would be subject to the annual Surprise Examination requirement. Moreover, because vastly more advisers (with exponentially more accounts) would be seeking Surprise Examinations, the demand for such audits will increase. We anticipate, however, that the supply of auditors willing and able to do this work may not increase as quickly.

It is, therefore, likely that audit firms will be in a position to raise the rates charged for this service.[8] In addition, there may be insufficient resources to assure that all advisers

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[7] *2009 Release*, *supra* note 1.

[8] Ordinarily, the increased costs will be passed along to clients. Where that is not possible, the adviser itself will need to bear the increased costs, which is likely to have a disparate impact on smaller advisers. Moreover, it is possible that certain areas of the U.S. will have less access to capable accountants that can perform a Surprise Examination and that non-U.S. advisers may have no access to PCAOB-registered accounting firms to provide services required to be provided by such firms under the Custody Rule. In those cases, costs will be further increased by the need for the auditor to incur travel costs (which, again, would be borne by the adviser or its clients) in order to conduct the Surprise Examination. Again, this will likely have a disparate impact on smaller advisers who are more likely to be located outside of the major financial centers.

Finally, as discussed below, recent legislative initiatives, if enacted, would require the registration of nearly all domestic (and many foreign) advisers to private funds. Most, if not all, of these potential new registrants will be deemed to have custody and will be competing for the services of accounting firms in performing audits and Surprise Examinations further increasing the demand for (and, likely, the cost of) these services.

who need to undergo an annual Surprise Examination will be able to do so timely. This will be exacerbated by the Proposed Amendments in that (i) the release seems to increase the burden imposed in connection with the audit work and (ii) the Proposed Amendments decrease the amount of time allotted for the audit firm to complete the Surprise Examination and file Form ADV-E.[9]

Prior to the 2003 amendments to the Custody Rule, most advisers who had automatic deduction authority were able to rely on no-action guidance from the Commission staff to avoid being deemed to have custody for purpose of the Custody Rule.[10] Moreover, when the Custody Rule was amended in 2003, the Commission recognized that deemed custody as a result of automatic debiting arrangements differed from circumstances where the adviser had greater access to client assets (*e.g.*, where the adviser had actual possession of client funds or securities) by, for example, (i) not requiring advisers who have custody solely as a result of automatic debiting of client accounts to declare that

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9 Currently, Rule 206(4)-2(a)(3)(ii)(B) under the Advisers Act requires that, among other things, (i) the Surprise Examination occur "at least once during each calendar year at a time that is chosen by the accountant" and (ii) the accountant performing the Surprise Examination "files a certificate on Form ADV-E . . . within 30 days after completion of the [Surprise E]xamination." Thus, under the current Rule, there is no explicit timeframe for completion of the Surprise Examination as the Form ADV-E deadline is tied to the completion, rather than commencement, of the Surprise Examination. By contrast, while the Proposed Amendments would continue to require that the timing of the Surprise Examination be "chosen by the accountant," the accountant would be limited in the amount of time allotted to complete the Surprise Examination, as Form ADV-E would be required to be "file[d] . . . within 120 days of the time chosen by the accountant [to commence the Surprise Examination]." *See*, Proposed Rule 206(4)-2(a)(4)(i) under the Advisers Act. The SEC indicated that it chose the 120-day period to reflect "the period of time in which a pooled investment vehicle managed by an adviser relying on the rule's annual audit exception must distribute its audited financial statements to investors in the pool." *2009 Release*, *supra* note 1, at text accompanying n. 28.

The 2009 Release also notes that the SEC's "examination staff has found that an adviser's [S]urprise [E]xamination may sometimes continue for an extended period of time." As discussed in more detail below, Surprise Examinations may be a costly and time consuming endeavor for certain types of accounts including, particularly, private funds of funds which, unlike other pools, are currently given a 180-day period to complete and distribute audited financial statements. We believe that 120 days may be an insufficient amount of time for an accountant to complete a Surprise Examination and file Form ADV-E and we urge the SEC to reconsider this deadline.

10 See *Custody of Funds or Securities of Clients by Investment Advisers*, Rel. No. IA-2044 (July 18, 2002) ("*2002 Proposing Release*") at n. 23 (citing *Investment Counsel Association of America, Inc.* (pub. avail. June 9, 1982); *John B. Kennedy* (pub. avail. June 5, 1996); and *Securities America Advisors Inc.* (pub. avail. Apr. 4, 1997)).

they have custody on Form ADV;[11] (ii) seeking to tailor the Custody Rule to assure that the requirements associated with this form of custody were commensurate with the risks associated with direct billing arrangements so that advisers having this form of custody would not be subject to unnecessary burdens;[12] and (iii) specifically indicating that "an adviser that has 'custody' for purposes of [the Rule] may not necessarily have custody for other purposes."[13]

As a result, under the current Custody Rule, such advisers generally are able to avoid the most burdensome aspect of the Rule (*i.e.*, the annual Surprise Examination) by assuring that clients receive quarterly (or more frequent) custodial statements from a qualified custodian so that "clients may confirm that the adviser has not withdrawn amounts in excess of its fee."[14] In both the proposing and adopting releases for the 2003 amendments to the Custody Rule, the Commission questioned the value of annual Surprise Examinations in these circumstances since "[r]eceiving quarterly statements directly from the qualified custodians will enable advisory clients to identify questionable transactions early and allow them to move more swiftly than relying on an annual Surprise Examination."[15] We note that the Proposed Amendments would reinforce the need for clients to review their account statements in a prompt and diligent manner by requiring advisers to include in notices sent to clients, when a new custodial account is

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11 Item 9 of Form ADV, Part 1, which inquires as to certain information about an adviser's custodial arrangements, states that an SEC registered adviser that:

> deduct[s its] advisory fees directly from [its] clients' accounts but . . . do[es] not otherwise have custody of [its] clients' funds or securities . . . may answer 'no' to Item 9A.(1) and 9A.(2).

This instruction was amended when the 2003 amendments to the Custody Rule were adopted. *See Custody of Funds or Securities of Clients by Investment Advisers*, Rel. No. IA-2176 (Sept. 25, 2003) ("*2003 Adopting Release*") (noting that the amendments to Form ADV were adopted "so advisers that have custody only because they deduct fees will not need to amend their registration statements.")

12 In proposing the 2003 amendments, the SEC noted that "[w]e have designed the proposed rule, so that these advisers would be able to comply with the rule without facing the burdens they previously sought to avoid." *2002 Proposing Release*, *supra* note 10, at n. 23.

13 *2003 Adopting Release*, *supra* note 11, at n. 12. The SEC intended the Rule to "define 'custody' broadly . . . to ensure that advisory clients receive reports on transactions and thus can take action to protect themselves in the event of an adviser's misuse of their funds." *Id.*

14 *Id.* at text accompanying n. 12.

15 *2003 Adopting Release*, *supra* note 11, at text following n. 55.

established by the adviser on a client's behalf or when certain information related to existing custodial accounts is changed, "a statement . . . urging clients to compare the account statements they receive from the [qualified] custodian with those they receive from the adviser."[16] As the Commission recognized in the prior releases, clients who promptly and carefully review account statements will be in a position to discover and react to inconsistencies no less frequently than quarterly; by contrast, clients would be in a position to react to an annual Surprise Examination only annually, if at all.

While we understand that there have been isolated instances of fraud involving advisers who were deemed to have custody of client assets as a result of direct billing arrangements, we do not believe that an annual Surprise Examination provides any real benefit in these circumstances – particularly where the custodian is independent of the adviser – as the limited access that advisers have to client assets as a result of direct billing makes it unlikely that client assets could be misappropriated through direct billing.[17] As the Commission has recognized, for most separately managed accounts, the client (and not the adviser) is responsible for selecting the custodian and managing the custodial relationship.[18] Where an adviser (i) does not mandate the use of particular (or even recommend) custodians, (ii) does not negotiate the terms of the custodial arrangements, and (iii) is not a party to the custody agreement, the adviser is typically limited to directing the custodian to take certain actions (such as to deliver funds or

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16 *2009 Release*, *supra* note 1, at text accompanying n. 63. *See also*, Proposed Rule 206(4)-2(a)(2) (requiring that notices provided to clients in connection with the opening of or changes to custodial accounts "[i]nclude . . . a statement urging clients to compare the account statements he or she shall receive from the [qualified] custodian with those from the adviser.").

17 As noted above, we are unaware of any settled or final enforcement action founded solely or principally on an adviser's misuse of the power to deduct fees. We believe that this is a risk primarily where the custodian is affiliated with the adviser. Under the Proposed Custody Rule, advisers using an affiliated custodian would have custody, regardless of billing arrangements. We note that the SEC requested comment as to whether all advisers should be required to use an independent custodian. While we believe that the use of an independent custodian provides significant protections to clients, we believe that prohibiting the use of self- or affiliate-custody would cause harm well in excess of the protections provided. In particular, a ban on custody of client assets by an adviser or an adviser's affiliate would require the radical restructuring of most wrap fee programs.

18 *See, e.g.*, *Commission Guidance regarding Client Commission Practices under Section 28(e) of the Securities Exchange Act of 1934,* Rel. No. 34-54165 (Jul. 18, 2006) (noting that "advisory clients, rather than [advisers], typically enter into contractual arrangements directly with custodians for their services.").

securities on a delivery versus payment ("DvP") basis or deduct fees) in accordance with procedures established by the client and the custodian, which further reduces the opportunity for fraud and misappropriation.

We believe that the protections incorporated in the existing Custody Rule, together with: (i) the use of a qualified custodian that is independent of the adviser; and (ii) the proposed enhanced notice to clients regarding the importance of reviewing and comparing their account statements,[19] are and will remain sufficient to assure that such advisers do not improperly deduct excess fees from client accounts. Moreover, we do not believe that most clients equate automatic deductions of advisory fees to actual, physical custody of client assets – after all, many of these same clients use automatic deduction arrangements to pay their mortgage, phone and cable bills without concern that the bank, phone company or cable provider will deduct an excessive amount of fees. Consequently, we believe it would be more appropriate to define custody to not include client accounts having automatic debiting arrangements in instances in which (i) the qualified custodian is independent of the adviser and (ii) the adviser to such accounts assures that clients receive quarterly (or more frequent) custodial statements from the qualified custodian.

The Surprise Examination is focused on confirming the existence and safekeeping of assets. It is our understanding that an accountant performing a Surprise Examination is not required to verify that the agreed-upon fee was charged. Thus, putting aside the potential deterrent effect, an annual Surprise Examination cannot prevent an adviser from overbilling. We believe that other, less burdensome, means than Surprise Examinations may actually be more effective at preventing billing fraud. Therefore, we suggest that if the Commission determines to continue to include automatic billing arrangements within the scope of the definition of custody, instead of mandating an annual Surprise Examination, the Custody Rule should require (i) the maintenance of assets with and provision of account statements by a qualified independent custodian and (ii) that the adviser enter into an agreement with the custodian that (a) requires the adviser to provide to the custodian the manner in which the fee is calculated for each account and (b) prohibits the custodian from disbursing funds in excess of the calculated fee. Additionally, we would suggest that the Commission specifically affirm the staff's position that where the client instructs its independent custodian to debit the client account and the custodian (rather than the adviser) calculates the fee based on the

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[19] *See supra* note 16 and accompanying text.

advisory contract without receiving a fee bill from the adviser, "the custodian is acting only as agent for the client, and the adviser does not have [custody]."[20]

We believe that many advisers will no longer offer automatic debiting if doing so will subject them to annual Surprise Examinations. Adopting one or more of the alternatives described above will enable advisers and clients to continue to enjoy the convenience and certainty commensurate with automatic billing arrangements while providing clients with protection from unscrupulous advisers who might seek to withdraw fees in excess of the amount due under the relevant advisory contract.

The Commission should clarify that advisers are not required to provide account statements to clients separate and apart from those provided by the qualified custodian

We note one potential inconsistency in the Proposed Custody Rule. While the Custody Rule does not appear to require advisers to send account statements to their clients, the enhanced notice requirement (described above) suggests that all advisers who have custody will send such statements to their clients. While we support the enhanced notice requirement, we believe that the related provision of the Proposed Custody Rule should be rephrased (or the adopting release should clearly indicate) that: (i) advisers are not required to send their own account statements to clients and (ii) the enhanced notice requirement only applies to advisers that choose to send their own account statements to clients.[21] Requiring this language to be used by advisers that do not choose to send their own account statements would result in unnecessary confusion for clients.

Circumstances where an affiliate has custody should create a rebuttable presumption of custody

While we agree that in many circumstances when an adviser or its affiliate acts as qualified custodian for an advisory account the adviser will have greater access to client assets, thereby increasing the risk of misappropriation, this is by no means universally true. Increased consolidation in the financial services industry means that a far larger number of advisers may have affiliates that may be engaged by a client to act as the

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[20] *Custody FAQ*, *supra* note 4, at Q III.3.

[21] The SEC also requested comment as to whether a similar legend should be included on any account statements that are sent by the adviser. We would support such a requirement.

client's custodian. As a result, we believe that the use of an affiliate as custodian with respect to a discretionary advisory account[22] should present a rebuttable presumption that the adviser has ready access to the account and, therefore, deemed to have custody. Whether or not the presumption holds with respect to any particular adviser would, in our view, depend on a balance of facts and circumstances as to the likelihood that (i) an adviser has actual access to client assets and (ii) there is an actual risk of loss or misappropriation.

Among the factors that might allow for a determination that an affiliate's custody of advisory assets should not be imputed to the adviser are: (i) whether client assets may be subject to claims by creditors of the adviser; (ii) whether advisory personnel have any real opportunity to misappropriate client assets; (iii) whether advisory personnel have actual custody, possession or access to client assets or the power to dispose of them for the benefit of the adviser; (iv) whether advisory and custodial personnel are under common supervision; (v) whether the adviser and custodian share personnel or premises and, if so, have access to client assets;[23] (vi) whether the affiliated custodian is in the business of providing services as an independent custodian to third-party advisers and the portion of the total assets under custody that are attributed to such business; (vii) the overall corporate structure and the distance between the custody function and the advisory function; (viii) whether the custodial entity is dominated by control persons of the advisory entity; (ix) whether significant regulatory, contractual or procedural controls exist to protect assets; (x) whether the adviser recommended or required its clients to use its affiliated custodian; (xi) whether the adviser is authorized to order withdrawals or transactions on an other than DvP basis; and (xii) with respect to advisers to private funds, whether the private fund retains an independent, third-party administrator or similar service provider.

In circumstances where there is little risk of misappropriation, we believe that the burdens associated with advisers being deemed to have custody bear little relationship to any benefit. We also believe that, even in circumstances where there is some risk of

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22 In a non-discretionary arrangement, the adviser does not have authority to execute trades or withdraw assets without client consent. Therefore, there is a much lower risk of misappropriation. As a result, we do not believe that a non-discretionary adviser whose clients happen to use an affiliated custodian should be deemed to have custody under the Custody Rule.

23 *See Crocker Investment Management Corp.* (pub. avail. Dec. 5, 1977) (describing circumstances where an affiliate's custody of client assets will not be imputed to the adviser).

misappropriation, the requirements of the Rule or the expectations of the Commission could be better tailored to reduce the burdens on advisers without materially increasing the risk to clients. For example, we expect that preparation of a written control report by the affiliate will be both burdensome and expensive. To the extent that a custodian is subject to regulatory requirements that are similar in nature to the internal control report, we would suggest that the Commission allow such reports to be used in lieu of an internal control report. Finally, we suggest that a reasonable transition period of at least 18 months be applied to the internal control report requirement to allow for coordination among advisers, accounting firms and qualified custodians as to the nature and content of these reports and to allow advisers and qualified custodians ample time to install appropriate internal controls.

APPLICATION TO ADVISERS TO PRIVATE FUNDS

Alternatives to the Surprise Examination should be available to advisers of private funds, to the extent that such alternatives provide equal or better protection, as Surprise Examinations may present particular difficulties for certain types of private funds

A significant number of advisers are subject to the current Custody Rule because they, or their affiliates, serve as general partner or managing member of a private fund. Most of these investment advisers deliver, on an annual basis, the fund's financial statements, audited in accordance with GAAP, to fund investors ("Audit Method") to comply with the current Custody Rule and to remain eligible for certain exemptions and exceptions from the current Custody Rule's requirements. Even where the Custody Rule is not implicated, it is common industry practice for private funds (including private funds of funds and private equity funds) to conduct and distribute annual audits to investors in the private fund for the purpose of keeping investors informed of the financial condition of the fund. In many cases, such audits are required by the private fund's governing documents.

Private funds invest in a wide variety of assets and employ a wide variety of structures. The current Custody Rule allows for the fact that these differing structures and investments may cause certain means of compliance to be more costly or difficult by allowing two options for advisers to private funds to comply with the Rule. First, an adviser can cause account statements "identifying the amount of funds and of each security in the account at the end of the period and setting forth all transactions in the account during that period"[24] to be sent to each investor in the private fund ("Account Statement Method").[25] Alternately, the adviser can rely on the Audit Method by assuring that the private fund undergoes an annual audit and that the related audited financial statements, prepared in accordance with GAAP, are provided to investors within a prescribed period.[26] The Rule currently includes a preference for the latter method, as advisers relying on the Audit Method are exempt from the requirement to assure that privately offered and uncertificated securities are held by a qualified custodian.[27]

The Proposed Rule would create particular compliance difficulties for private funds of funds. This is the case because of the particular methods of recording and tracking the securities held by private funds of funds and private equity funds. The assets of these

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[24] We understand that the SEC and its Staff interpret this requirement, with respect to private funds, to require the account statements to identify all assets and each transaction by the fund rather than transactions in any investor's capital account. *Custody FAQ*, *supra* note 4, at Q VI.2. As discussed below, we believe that private fund advisers should be required to provide different information to investors than is required to be provided to separate account clients as the information currently required to be included in account statements is not well suited to, and is likely to confuse or overwhelm, investors in private funds.

[25] As with other types of advisers, unless the statements are sent through a qualified custodian, a Surprise Examination would be necessary. We believe that many private fund advisers would choose to use an independent third-party administrator to distribute statements rather than the qualified custodian. For purposes of the Account Statement Method or any account statement delivery requirements that may be imposed by the Proposed Custody Rule, we believe that account statements prepared and delivered by a independent, third-party administrator, which are based on information provided by the qualified custodian or provided by the adviser or another party and verified by the qualified custodian or the independent, third-party administrator, should be treated the same for private fund advisers as those sent by the qualified custodian in the separate account context.

[26] Rule 206(4)-2(b)(3) under the Advisers Act. As discussed below, we agree that an annual audit can provide reasonable protections for investors. However, the requirement that the audit be "in accordance with GAAP" has caused a number of advisers to avoid the Audit Method where they may be able to obtain an audit only with immaterial deviations from GAAP or where, due to the nature of underlying funds (or the timing of those funds' audits) it proves impossible to complete the audit and distribute the financial statements within the time limits set forth by the Rule. We believe that the Rule should provide a mechanism for appropriate relief to allow for delays in the audit or immaterial deviations outside the advisers' control. Such a mechanism could broaden the class of investors who receive the benefit of an annual GAAP audit.

[27] Rule 206(4)-2(b)(2)(ii) under the Advisers Act.

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private funds (whether they are interests in other private funds or are securities of private companies) are not typically certificated or registered in the name of a third-party custodian. Instead, a private fund of fund's interest in, or shares of, an underlying private fund are uncertificated and memorialized only by a notation in the records of a third-party administrator or transfer agent for the underlying private fund, or in some cases, on the list of investors maintained by the underlying private fund itself. Similarly, a private equity fund's interest in a private company may only be noted on the books of the transfer agent of that company or by the company itself.

As the Commission staff has acknowledged in the past, private funds of funds depend on the availability of the audited financial statements of the underlying private funds in which they invest in order to accurately and meaningfully audit their own holdings.[28] The existing system is practical and efficient, in most cases, because virtually all private funds, private funds of funds and private equity funds operate on a calendar fiscal year. Surprise Examinations, however, by their very nature, are not permitted to be performed on a regular or predictable schedule.[29] Absent reliance on audits of the underlying private funds, we would anticipate that independent public accountants conducting a Surprise Examination would seek to obtain individual confirmations from the adviser of each underlying private fund or the corporate transfer agents that their records are consistent with those of the private fund of funds or the private equity fund. In the case of a private fund of funds, this would require the cooperation of each underlying private fund's adviser to obtain this data. Although many underlying private fund advisers would cooperate, some may not. Absent an amendment to most underlying private funds' governing documents, the adviser of a private fund of funds could not compel underlying private funds or their advisers to cooperate with the independent public accountant conducting a Surprise Examination. Unless the private fund of funds could compel cooperation with the private fund of fund's independent public accountant, the adviser to a private fund of funds might not be able to comply with the requirements of the Proposed Custody Rule. Moreover, it would be very expensive and burdensome to ask every company with privately issued shares to open their books to the auditor of a private equity fund.

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28 *American Bar Association* (pub. avail. Aug. 10, 2006) ("*ABA*").

29 *See, e.g., In the Matter of Kaufman, Bernstein, Oberman, Tivoli & Miller, LLC and Howard M. Bernstein,* Rel. No. IA-2194 (Nov. 20, 2003) (finding a violation of the Custody Rule where "the predictable timing of the examinations . . . effectively put [the adviser] on notice that the [Surprise E]xaminations would begin in the first few days of January each year.").

The complications of performing a Surprise Examination of a private fund of funds, alone, are likely to add significantly to the costs of such an examination – costs which will likely be borne by investors.[30] However, there is another factor that could also greatly increase costs beyond the amount estimated in the Commission's cost/benefit analysis – the increased number of advisers competing for services as a result of both the Proposed Amendments and the current initiatives to require the registration of thousands of additional private fund advisers.[31] If these are adopted, we can expect that the cost of annual GAAP audits and annual Surprise Examinations, as well as the difficulty in meeting regulatory deadlines, will increase as more and more advisers compete for the services of a limited number of providers.

We believe that the potential added benefits of imposing the Surprise Examination requirement on advisers who are deemed to have custody solely as a result of serving as a private fund's general partner or managing member (or having an affiliate serve in such a role) are unlikely to be commensurate with the cost imposed on the private funds, their advisers and their investors. Private funds and their advisers are subject to the full anti-fraud requirements of the law and the Commission has broad investigative authority pertaining to their activities. Additionally, the Commission currently has examination authority with respect to registered advisers and a number of legislative proposals have been considered which, if enacted, would extend this examination authority to nearly all domestic private fund advisers and many foreign private fund advisers. As noted previously, this could greatly increase the costs of a GAAP annual audit for advisers electing the Audit Method and of a Surprise Examination for those advisers who would be subject to the Surprise Examination requirement and put pressure on the timing requirements that are imposed by the current Custody Rule and that would be imposed by the Proposed Amendments.

Considering the reason for the Surprise Examination (*i.e.*, to assure the existence and safekeeping of the assets of the private fund) and the cost factors already cited, we believe that a better approach would be to offer advisers to private funds multiple avenues for compliance and allow each adviser to determine, with respect to each private fund, the best and most cost effective alternative for that private fund. We believe that, in

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30 The cost associated with an audit is typically a private fund expense, which is borne, indirectly, by investors in the private fund.

31 *See supra* notes 7 and 8 and accompanying text.

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addition to the options that would be offered by the Proposed Amendments,[32] the Commission should permit private fund advisers to (i) provide both an annual audited financial statements and quarterly account statements and (ii) assure that the private fund's assets (including uncertificated securities) are held by an independent qualified custodian (*i.e.*, one which is not affiliated with the private fund's adviser) in lieu of the annual Surprise Examination. Subjecting private funds of funds, private equity funds and other private funds to Surprise Examinations, without providing for this potentially equally effective but less burdensome option, would place an impractical and costly burden on the operations of these entities.

Account statements for private fund advisers relying on the "Account Statement Method" should be better tailored to serve the purposes of the Rule and the nature of private funds

The alternative proposed above (and the Account Statement Method in general) would be of most utility in the private fund context if investors are provided with account statements that are (i) meaningful to them, given the nature of the investment, and (ii) not overly complex. An investment in a private fund is qualitatively different from the establishment of a separate account advisory relationship. Investors in a private fund do not generally have a direct ownership interest in the private fund's assets but, rather, own an interest in the private fund as a whole. By contrast, the separate account owner actually owns an undivided interest in each of the underlying securities. Moreover, many private funds trade far more frequently than separate accounts. For some private funds, such investors would receive literally hundreds of pages of transactions – an amount of data that would likely be overwhelming and thus would prevent the effective discovery of transactions that might indicate that the adviser is misappropriating client assets. As a result, the information required by the Custody Rule to be included in account statements[33] is likely to be of limited utility, overwhelming and confusing for many investors in private funds.[34] For private fund investors, account statements that mirror

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32 *I.e.*, (i) Audit Method and a Surprise Examination and (ii) Account Statement Method and a Surprise Examination.

33 Rule 206(4)-2(a)(3) under the Advisers Act. The current Custody Rule requires quarterly account statements "identifying the amount of funds and of each security in the account at the end of the period and setting forth all transactions in the account during that period."

34 Similarly private funds that invest in unregistered securities of operating companies (*e.g.*, "buy-out" funds) may have difficulty reporting as the interests would need to fair value these assets quarterly.

those required for separate account clients would obfuscate, rather than disclose, useful information, making it very difficult to identify any possible misappropriation of the private fund's assets by its adviser. Nonetheless, the Proposed Rule would treat investors in private funds identically to separate account clients for purposes of the Account Statement Method.

The option to elect the Account Statement Method, the Audit Method or, if the Commission adopts our suggestion above, another alternative, is valuable to advisers, to private funds and to their investors. We believe, however, that the Account Statement Method (or an alternative that involves the delivery of account statements) would be beneficial if the account statements provide meaningful information in furtherance of the anti-fraud goals of the Rule. In order for this to be the case, we believe that the nature of the information required in such statements must be significantly improved. We recommend that quarterly statements for private funds reflect the status of the holdings of the private fund at the beginning and the end of the quarter, with a materiality threshold for position level disclosure (*e.g.*, 5% of net asset value); as well as any payments to the adviser or any service provider (other than transaction related payments such as brokerage commissions and routine payments such as audit fees, legal fees and taxes).[35] This change should make statements less complex, more effective and more meaningful to investors.

Alternately, the Commission could improve account statements by requiring or allowing advisers to private funds to cause to be distributed to each investor information about that investor's position (*e.g.*, percent interest, total value of the private fund and net asset value), coupled with more useful summary information about the private fund that should help the investor to better understand the nature of his investment and to detect potential misuse or misappropriation of assets such as: aggregate inflows and outflows; total securities sold and purchased; a listing of the top ten securities or securities having a value in excess of 5% of the private fund's net asset value at the end of the period; and fees paid to the adviser and other service providers. This would increase efficiency,

While FAS 157 requires annual fair valuation in connection with the GAAP audit (for private funds relying on the Audit Method), it does not require that these be marked quarterly, increasing costs.

[35] Advisers should also be permitted, with the approval of investors, to exclude certain holdings for legitimate reasons (*e.g.*, assuring confidentiality for certain positions if confidentiality is crucial to the strategy).

decrease costs, and provide investors in private funds with more meaningful information to monitor the assets held by, and performance of, the private funds in which they invest without diminishing the investor protection goals of the Rule. We believe that this approach would be more useful and cost effective than an annual Surprise Examination.

The Commission should return to the Rule the ability for Funds of Funds to distribute their audit reports within 180 days rather than 120 days

Ignoring prior changes made to the Custody Rule that differentiated between private funds of funds and other types of private funds and facilitated the ability of private funds of funds to rely upon audits performed on underlying private funds in connection with the private fund of fund's audit, the Proposed Custody Rule does not define "fund of funds" and would subject all private funds to a 120-day deadline for purposes of the Audit Method. This is a significant change since many private funds of funds seek to rely on the Audit Method (despite its difficulties) in order to be eligible for an exception from the qualified custodian requirement with respect to certain types of uncertificated securities.[36] The 2009 Release, however, neither explains nor references the omission of the 180-day provision for private funds of funds and the definition of "fund of funds."[37] While we believe that this was an inadvertent omission, we comment to emphasize the importance of this additional time for private funds of funds to complete their audits.[38]

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[36] Rule 206(4)-2(b)(2)(i) under the Advisers Act. This provision of the Rule excepts from the qualified custodian requirement securities that are:

> (A) acquired from the issuer in a transaction or chain of transactions not involving any public offering;
>
> (B) uncertificated, and ownership thereof is recorded only on the books of the issuer or its transfer agent in the name of the [fund]; and
>
> (C) transferable only with the prior consent of the issuer or holders of the outstanding securities of the issuer.

Rule 206(4)-2(b)(2)(ii) under the Advisers Act excludes advisers to private funds from relying on this exception unless they also comply with the Audit Method. Accordingly, the cost of compliance with the Proposed Custody Rule, should a fund of funds lose its ability to rely on the audit delivery provision of the Rule, would be considerable indeed if the 180-day period is not restored.

[37] Rule 206(4)-2(c)(4) under the Advisers Act.

[38] We understand that an annual audit of a private fund of funds consists, primarily, of the review and integration of information derived from the audited financial statements of the underlying private

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The extended compliance period for private funds of funds was included in the current Rule in order to accommodate the practical constraints facing these entities.[39] Because the annual audits of private funds of funds necessarily depend on their ability to obtain audits from the underlying private funds in which they invest, it would be very difficult, if not impossible, for private funds of funds to complete an annual audit in a timely fashion if the annual audit must be completed within the same time frame as that for its underlying private fund holdings. Thus, under the Proposed Custody Rule, private fund of funds effectively would be: (i) precluded from relying on the Audit Method and, instead, be required to rely on the Account Statement Method; and (ii) unable to rely on an exception allowing private funds using the Audit Method to avoid maintaining uncertificated and privately offered securities with a qualified custodian.

The Commission's provision for staggered compliance periods to accommodate the industry was overwhelmingly commended by commentators when proposed in 2004.[40] Moreover, the Commission staff has acknowledged the valuable purpose that this provision serves, stating that the adoption of the 180-day audit period "was designed to address the practical difficulties faced by advisers to funds of funds in obtaining completion of their final fund audits prior to completion of the audits for the underlying funds in which they invest."[41]

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funds. See discussion above regarding the difficulties of completing a private fund of fund's audit when underlying private fund's audits are not yet available.

39 *See Registration under the Advisers Act for Certain Hedge Fund Advisers*, Rel. No. IA-2333 (Dec. 10, 2004) ("*Hedge Fund Advisers Release*"). The Hedge Fund Advisers Release and, presumedly, all of the rule amendments adopted in that release were subsequently vacated by the decision of the DC Circuit. *See Goldstein et al. v. Securities and Exchange Commission*, 451 F.3d 873, Fed. Sec. L. Rep. (CCH) P 93890 (D.C. Cir. 2006) ("*Goldstein*"). Subsequently, in a 2006 no-action letter, the SEC staff stated that it would continue to observe the 120-day/180-day distinction provided in the rule, without passing on the potential legal issues created for the Hedge Fund Rule by the *Goldstein* decision. See *ABA*, *supra* note 28.

40 *See Hedge Fund Advisers Release*, *supra* note 39.

41 *ABA*, *supra* note 28.

The Rule should provide for relief (or a relief mechanism) where the adviser is unable to obtain a fully GAAP-compliant audit or distribute the audited financial statements in a timely manner through no fault of its own

We recommend that the Proposed Custody Rule be revised to permit advisers to private funds, private funds of funds and private equity funds that make a good faith effort to comply with the Audit Method but, due to reasons beyond the adviser's reasonable control, are unable to (i) complete audits within the prescribed periods or (ii) obtain a fully GAAP-compliant audit due to certain immaterial deviations, nonetheless, to rely on the Audit Method. This is particularly important because, by the time an adviser discovers that a private fund's audit will be non-compliant or untimely, its ability to rely on an alternate method may be compromised (*e.g.*, the adviser may not have caused quarterly account statements to be delivered if it anticipated relying on the Audit Method).

To deal with audits that cannot be completed timely, a mechanism should exist for the Commission or its staff to issue extensions for good cause shown where the failure to meet the deadline is beyond the adviser's reasonable control (*e.g.*, the inability of a private fund of funds to receive timely financial statements from one of the underlying private funds in which it has invested). We believe that such a mechanism could be modeled on that employed by the Commodity Futures Trading Commission ("CFTC").[42] This would supplement existing guidance provided by the Commission staff with respect to non-timely audits.[43]

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[42] *See* CFTC Rule 4.7(e). Under CFTC rules, commodity pool operators must annually furnish independently certified, GAAP-compliant account statements to pool participants. *See* CFTC Rules 4.22(c) and (d). However, an exemption is available to those pool operators who electronically file modified annual reports with the National Futures Association within 90 days of the end of the pool's fiscal year. *See* CFTC Rule 4.7(b)(3)(i). Commodity pools that cannot file these reports within 90 days of the end of the fiscal year do not lose their exemption so long as "[a] good faith and reasonable attempt was made to comply with all applicable terms, conditions and requirements" of the regulation that provides the exemption. CFTC Rule 4.7(e)(iii).

[43] *See Custody FAQ*, *supra* note 4, at Q. VI.9 (stating that "[t]he Division [of Investment Management] would not recommend enforcement action for a violation of rule 206(4)-2 against an adviser that is relying on rule 206(4)-2(b)(3) and that reasonably believed that the private fund's audited financial statements would be distributed within the . . . deadline"). We believe that, at a minimum, this aspect of the Custody FAQ should be incorporated into the Custody Rule and/or specifically referenced in any related adopting release.

While the Commission staff has provided some comfort to advisers who may discover, too late, that an audit will not be timely,[44] neither the Commission nor its staff has provided similar guidance for the most common immaterial deviations from GAAP that could arise for private funds.[45] We recommend that some relief be provided in circumstances where a deviation from GAAP does not materially affect the validity of the audit, result in misleading financials or threaten the investor-protection goals of the Custody Rule. Examples might include, but should not be limited to, circumstances where the inability to obtain a fully GAAP-compliant audit is attributable to: (i) the failure of one or more underlying private funds to provide GAAP-compliant financial statements;[46] (ii) the private fund amortizes start-up costs in a manner that is inconsistent with GAAP; (iii) illiquid, side-pocket investments not having been fair valued; and (iv) deviation from certain FAS 157 requirements.[47] In the latter three cases, we believe that the intent to amortize start-up costs or refrain from fair valuing assets should be clearly reflected in the fund's offering or governing documents.

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[44] *See* note 43, *supra*.

[45] We note, however, that the 2003 Adopting Release does provide relief from the GAAP requirement in the limited instance where the private fund is organized outside of the U.S. or the general partner or other adviser has a principal place of outside the U.S. provided that the "financial statements contain information that is substantially similar to financial statements prepared in accordance with U.S. GAAP and contain a footnote reconciling any material variations between [the relevant] comprehensive body of accounting standards [used for the fund's audit] and U.S. GAAP." *2003 Adopting Release*, *supra* note 11, at n. 41. We would suggest that this exception be retained and codified in the Proposed Custody Rule.

[46] Many private equity and other private funds do not provide and are not required to provide GAAP-compliant financials. For the reasons discussed above, it may be difficult for private funds that invest in such entities to prepare GAAP-compliant financials. *See* "Alternatives to the Surprise Examination should be available to advisers of private funds to the extent that such alternatives provide equal or better protection, as Surprise Examinations may present particular difficulty for certain types of private funds," *supra*.

[47] We would suggest that the SEC include in any adopting release or the Rule itself a non-exhaustive list of examples that are self-executing; provided that the auditor's opinion was delivered without material qualification. While we believe that the adviser and the auditor are in the best position to determine if a particular deviation is immaterial, the SEC could require advisers to provide notice to the staff of their intent to rely on this relief. If so, we would suggest that advisers be permitted to rely on the relief, for the year filed, if the adviser files in good faith. Alternately, the staff could be encouraged to consider no-action relief or promote interpretive guidance as to classes of deviations that would be considered immaterial for this purpose.

Valuation of privately offered securities by auditors should not become a requirement of the Custody Rule

The Commission also seeks comment on whether, in conjunction with its requirement for an annual Surprise Examination, the independent public accountant should be required to perform valuation testing on private funds.[48] While valuation is an important matter, we do not believe that it should be addressed in the Custody Rule, as valuation concerns apply also to advisers who do not have custody and who are not subject to the Rule. All advisers should be encouraged to adopt valuation procedures that are tailored to the nature of the assets in their client portfolios. Should a Surprise Examination of privately offered securities be required, the role of the auditor should be limited to an assessment of whether valuations are consistent with stated procedures and applicable law. Moreover, we do not believe that auditors are in the best position to pass judgment on an adviser's valuation methodologies and, in some instances, the adviser may not be the party responsible for valuation.[49]

Imposing a valuation requirement in connection with the Surprise Examination presents significant difficulties.[50] Private funds and separately managed accounts may invest in assets that are complex and difficult to value. Such assets often can be valued only through the use of sophisticated valuation techniques, often requiring the exercise of judgment. These techniques may be an important part of the expertise for which the investment adviser is retained. It would be expensive, duplicative, and inefficient to require an accountant to replicate these techniques, or to require a comparably trained analyst to duplicate the adviser's valuation processes.[51] Moreover, it is unlikely that accountants would be willing or able to perform this function.

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48 *See 2009 Release*, *supra* note 1.

49 If the SEC were to impose a valuation requirement, an adviser who does not have valuation authority over assets should be excepted.

50 In the case of private funds employing the Audit Method, valuation review may be duplicative as some testing of valuation processes against the adviser's procedures and applicable requirements is generally included in the annual, GAAP audit.

51 The SEC estimates that the average Surprise Examination will cost investment advisers approximately $8,100. Given the expansive nature of the inspection and valuation procedures that the SEC seeks to require as part of a Surprise Examination, it is unlikely that "costs could be contained to [the estimated] level if a fund is trading anything more complicated than large-cap, liquid [equity]

CONCLUSION

For the reasons set forth above, the Commission should continue to except advisers from the Surprise Examination requirement with respect to clients (i) who are private funds that are audited at least annually consistent with the Audit Method and (ii) for which the adviser has custody solely as a result of automatic billing arrangements. Furthermore, the Commission should preserve the 180-day compliance period permitted to private funds of funds in order to complete the annual audits currently necessary for them to obtain this and other exemptions available under the Custody Rule. Guidance or relief to private funds that are unable to comply with the annual audit requirement, even after a good faith effort to do so, should be continued in the final Custody Rule (as it is permitted in the current Custody Rule). To increase the goals of investor protection, while simultaneously improving efficiency and lowering costs to investors, the Commission should also consider the potential benefits of modifying the information that is required to be included in quarterly account statements so that those statements are less cumbersome and more meaningful to the clients or investors that receive them. Finally, the Commission should not confuse valuation with safekeeping. Advisers should be encouraged and permitted to value and account for managed assets in the way best suited to those assets, without altering the adviser's status under the Custody Rule.

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We appreciate the opportunity to comment on the Proposed Amendments. If the Commission or its staff have any questions or wish to discuss the matters mentioned in this letter, please contact: Jane Kanter at 202.261.3302 or jane.kanter@dechert.com; George Mazin at 212.698.3570 or george.mazin@dechert.com; John O'Hanlon at 617.728.7111 or john.ohanlon@dechert.com; or Michael Sherman at 202.261.3449 or michael.sherman@dechert.com.

securities." Anna Snider, "What Does the Market Think of the SEC's Proposed Amendments to the Custody Rule," The Hedge Fund Law Report, Vol. 2. No. 21 (May 27, 2009). We believe that costs would increase even more substantially in these circumstances if a valuation requirement is included. These costs will be passed on to the investor with no appreciable benefit provided in return.

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Very truly yours,

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