



Office of the General Counsel

B-280637

August 5, 1998

The Honorable Alfonse M. D'Amato
Chairman
The Honorable Paul S. Sarbanes
Ranking Minority Member
Committee on Banking, Housing, and Urban Affairs
United States Senate

The Honorable Thomas J. Bliley, Jr.
Chairman
The Honorable John D. Dingell
Ranking Minority Member
Committee on Commerce
House of Representatives

Subject: Securities and Exchange Commission: Interpretation of Section 206(3) of the Investment Advisers Act of 1940

Pursuant to section 801(a)(2)(A) of title 5, United States Code, this is our report on a major rule issued by the Securities and Exchange Commission (SEC), entitled "Interpretation of Section 206(3) of the Investment Advisers Act of 1940" (Release No. IA-1732). We received the release on July 17, 1998. It was published in the Federal Register on July 23, 1998. 63 Fed. Reg. 39505.

The rule, issued by the SEC as an interpretative release, concerns section 206(3) of the Investment Advisers Act of 1940. Section 206(3) generally prohibits an adviser from engaging in or effecting principal or agency transactions with an advisory client unless the adviser discloses certain information and obtains the client's consent before completing the transaction. The release states that the transaction is complete upon settlement, not execution.

While this interpretative rule was not subject to the normal notice and comment procedures of the Administrative Procedure Act, the SEC and the Office of Information and Regulatory Affairs, Office of Management and Budget, have determined that it is a major rule under the Small Business Regulatory Enforcement

Fairness Act. The effective date has been delayed the required 60 days pending congressional review. 5 U.S.C. § 801(a)(3).

Enclosed is our assessment of the SEC's compliance with the procedural steps required by section 801(a)(1)(B)(i) through (iv) of title 5 with respect to the rule. Our review indicates that the SEC complied with the applicable requirements.

If you have any questions about this report, please contact James Vickers, Assistant General Counsel, at (202) 512-8210. The official responsible for GAO evaluation work relating to the Securities and Exchange Commission is Thomas McCool, Director, Financial Institutions and Markets Issues. Mr. McCool can be reached at (202) 512-8678.

Robert P. Murphy
General Counsel

Enclosure

cc: The Honorable Jonathan G. Katz
The Secretary of the Securities and
Exchange Commission

ANALYSIS UNDER 5 U.S.C. § 801(a)(1)(B)(i)-(iv) OF A MAJOR RULE
ISSUED BY
THE SECURITIES AND EXCHANGE COMMISSION
ENTITLED
"INTERPRETATION OF SECTION 206(3) OF THE
INVESTMENT ADVISERS ACT OF 1940"
(Release No. IA-1732)

(i) Cost-benefit analysis

The SEC was not required to prepare, nor did it prepare a cost-benefit analysis for the release.

(ii) Agency actions relevant to the Regulatory Flexibility Act, 5 U.S.C. §§ 603-605, 607, and 609

Since the release is not subject to the notice and comment procedures of the Administrative Procedure Act, the SEC was not required to do either an Initial or a Final Regulatory Flexibility Analysis.

(iii) Agency actions relevant to sections 202-205 of the Unfunded Mandates Reform Act of 1995, 2 U.S.C. §§ 1532-1535

As an independent regulatory agency, the SEC is not subject to title II of the Unfunded Mandates Reform Act of 1995.

(iv) Other relevant information or requirements under acts and executive orders

Administrative Procedure Act, 5 U.S.C. §§ 551 *et seq.*

Since the release is considered an interpretative rule under the Administrative Procedure Act, it is excepted from the notice and comment procedures found at 5 U.S.C. § 553.

Paperwork Reduction Act, 44 U.S.C. §§ 3501-3520

The release does not contain any information collections which are subject to review and approval by the Office of Management and Budget under the Paperwork Reduction Act.

Statutory authorization for the rule

The release was issued pursuant to section 206(3) of the Investment Advisers Act of 1940 (15 U.S.C. § 80b-6(3)).

Executive Order No. 12866

The rule, promulgated by an independent regulatory agency, is not subject to the review requirements of Executive Order No. 12866.