



DIVISION OF
INVESTMENT MANAGEMENT

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

ACT IAA
SECTION _____
RULE 204-2
PUBLIC
AVAILABILITY 7/21/97

July 21, 1997

Via Facsimile and Air Mail

Mr. John Fox
General Counsel
MLC Limited
105-153 Miller Street
North Sydney NSW 2060
Australia

Dear Mr. Fox:

In your letter dated June 18, 1997, you request information regarding (i) the requirements in our jurisdiction for keeping records of advice provided by an investment adviser to its clients and (ii) the incentives or deterrents that apply in relation to compliance with those requirements. As you know, the Division of Investment Management of the Securities and Exchange Commission regulates the activities of federally registered investment advisers pursuant to the Investment Advisers Act of 1940 (the "Advisers Act").¹

Under the Advisers Act, an investment adviser has a fiduciary duty to its clients and, as a fiduciary, must make suitable recommendations to its clients in light of their needs, financial circumstances and investment objectives.² Rule 204-2

¹Pursuant to the National Securities Markets Improvement Act of 1996 ("NSMIA"), an investment adviser that (i) manages, in the aggregate, accounts with less than \$25 million in assets and (ii) does not manage a registered investment company, is subject to state rather than federal regulation. Recordkeeping requirements vary from state to state and may differ from the federal requirements outlined below. The fiduciary duty of advisers to their clients applies, in general, to both state- and federally-registered investment advisers.

²In SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180 (1963), the U.S. Supreme Court held that Section 206 of the Advisers Act, the general anti-fraud provision of that Act, imposes a fiduciary duty on investment advisers. In 1994, the Commission proposed a rule under the Advisers Act to codify its long-standing interpretation that investment advisers have a duty to their clients to provide only suitable investment advice. Investment Advisers Act Release No. 1406 (March 16, 1994). Although the proposed rule has not been adopted (or withdrawn), the duty to provide suitable investment advice is enforceable by the Commission under the anti-fraud provisions of the Advisers Act.

Mr. John Fox
July 21, 1997
page 2

under the Advisers Act prescribes the specific requirements for maintaining records of investment advice.

Paragraph (a) (7) (A) of that rule requires an adviser to maintain originals of any and all written communications of recommendations and advice made or given (or proposed to be made or given), but does not require an adviser to put its recommendations or advice into writing. Paragraph (a) (11) requires an adviser to maintain a copy of communications circulated by the adviser to ten or more persons and, if the communication recommends the purchase or sale of a specific security and does not state the reasons for such recommendation, the adviser must maintain a memorandum indicating the reasons for the recommendation. Pursuant to paragraph (a) (3), an adviser must maintain a memorandum of each order given by the adviser for the purchase or sale of any security; the memorandum must show, among other things, the identity of the person who recommended the particular transaction effected by the adviser for the client. For your reference, a copy of the rule is enclosed with the air mail copy of this letter.

An adviser has varied incentives to comply with these recordkeeping requirements and to prepare written records of its investment advice. Failure by a registered investment adviser to comply with the requirements of Rule 204-2 may result in an enforcement action brought by the Commission in which the Commission would seek injunctive or other equitable relief, as well as the imposition of sanctions, such as a censure, suspension or revocation of the adviser's registration with the Commission and monetary penalties. Sanctions imposed in enforcement actions are a matter of public record and, depending on their severity, must be disclosed to clients and prospective clients.³ Furthermore, as a practical matter, maintenance by an adviser of written records of its advice could protect the adviser from spurious claims that its advice was not consistent with its fiduciary duty to its clients.

The provision of investment advice by a broker-dealer is subject to both the anti-fraud provisions of the Securities Exchange Act of 1934 (the "1934 Act") and the Conduct Rules of

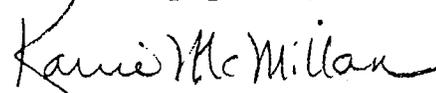
³Rule 206(4)-4. In addition, a client or prospective client may obtain from the Commission a copy of the adviser's registration on Form ADV, which is required to contain information concerning disciplinary proceedings against the adviser. Pursuant to Section 306 of NSMIA, a public system will be established to respond to inquiries regarding disciplinary actions and proceedings against investment advisers and persons associated with investment advisers.

Mr. John Fox
July 21, 1997
page 3

the National Association of Securities Dealers, Inc. ("NASD").⁴ Rule 2310 of the NASD's Conduct Rules requires an NASD member to obtain certain information about non-institutional customers prior to recommending a transaction to them, including a customer's financial status, tax-status, investment objectives and such other information used or considered to be reasonable by such member in making recommendations to the customer. Conduct Rule 3110(c) sets forth the recordkeeping requirements with respect to customer accounts.⁵ We suggest that you contact the NASD directly at (202) 728-8953 (fax: (202) 728-8894) for more information.

We hope this information is helpful. Please contact Alison M. Fuller in this office or me at (202) 942-0660 (fax: (202) 942-9659) if you have further questions.

Very truly yours,



Karrie H. McMillan
Special Counsel

enclosures (w/air mail copy)

⁴The Commission enforces the obligation of a broker-dealer to render suitable investment advice under Rule 10b-5 under the 1934 Act. A copy of the rule is enclosed with the air mail copy of this letter.

Broker-dealers are exempt from the definition of investment adviser set forth in Section 202(a)(11) of the Advisers Act, provided that the performance of advisory services by the broker-dealer is solely incidental to the conduct of its business and the broker-dealer receives no special compensation therefor. Broker-dealers that do not qualify for the exemption are subject to regulation under both the Advisers Act and the rules of the NASD. Most broker-dealers are required to be members of the NASD.

⁵IM-3110 of the Conduct Rules addresses the recordkeeping requirements relating to the information obtained pursuant to Conduct Rule 2310. Copies of Conduct Rules 2310 and 3110 and IM-3110 are enclosed with the air mail copy of this letter.



Facsimile

To	Karrie McMillan	Fax Number	0011 1 202 942 9659
Company	Securities and Exchange Commission		
From	John Fox	Phone Number	(612) 9957 8358
CC		Fax Number	
Date	18 June, 1997	Total pages including cover	
Subject	Requirements to maintain records of advice (Our Ref: 9/3, 9/10)		

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Dear Karrie,

Last year you kindly provided me with information about the regulation of securities advice in the United States. I would like to again ask your help.

- Our insurance and securities regulators are concerned with the difficulties faced by customers in obtaining compensation for damages suffered as a result of poor advice. In particular, they are concerned with the difficulties customers face in proving the terms of the advice given to them.

It is now proposed that our governing legislation be amended to reverse the onus of proof. There is to be a presumption that advice was not given at the required standard if an "adequate" written record of that advice is not produced by the agent or representative. The agent or representative will be able to provide evidence of the advice given so as to rebut the presumption.

I am writing to you on behalf of our industry organisation, the Life Investment and Superannuation Association of Australia, Inc ("LISA").

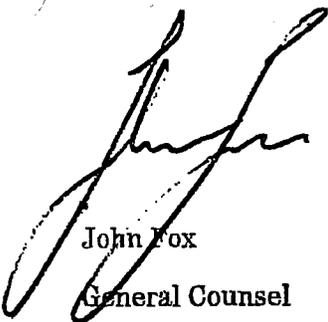
LISA opposes the proposed rebuttable presumption as an appropriate means of promoting record keeping. It believes that other, less draconian, measures should be developed.

We seek your advice as to the requirements governing record keeping in your jurisdiction and would be obliged if you told us:

- 1. whether there are any requirements for keeping records of advice in your jurisdiction; and*
- 2. if so:*
 - (a) what the terms of those requirements are; and*
 - (b) what incentives or deterrents apply in relation to compliance with those requirements.*

Unfortunately, we expect that we will only be given a very short time to consider the legislation and so ask that you respond as soon as possible. My fax number is (612) 9966 3295.

Yours Sincerely



John Fox
General Counsel