if there are signs of movement or if there are gaps under the head or collar.

(3) Do detailed inspections of the fasteners that hold the strut to the horizontal flange of the strut-to-diagonal brace fitting to determine if there are signs of movement or if there are gaps under the head or collar.

Exceptions to Alert Service Bulletin Procedures

(i) Where the alert service bulletin specifies a compliance time relative to ''the date on this service bulletin,'' this AD requires compliance within the corresponding specified time relative to the effective date of this AD.

(j) Where the alert service bulletin specifies a compliance time relative to the ''date of issuance of airworthiness certificate,'' this AD requires compliance within the corresponding time relative to the date of issuance of the original standard airworthiness certificate or the date of issuance of the original export certificate of airworthiness.

(k) If any crack is found during any inspection required by this AD, and the alert service bulletin specifies to contact Boeing for appropriate action: Before further flight, repair the crack using a method approved in accordance with the procedures specified in paragraph (o) of this AD

Credit for Actions Done Using Previous Service Information

(l) Actions done before the effective date of this AD in accordance with Boeing Service Bulletin 757–54A0047, Revision 1, dated March 24, 2005; and Boeing Alert Service Bulletin 757–54A0047, Revision 2, dated January 31, 2007; are considered acceptable for compliance with the corresponding actions specified in this AD.

(m) An inspection and corrective actions done before June 29, 2005 (the effective date of AD 2005–12–04), in accordance with paragraph (b) or (c), as applicable, of AD 2004–12–07, are acceptable for compliance with the initial inspection requirement of paragraph (h) of this AD.

An Acceptable Method of Compliance With Certain Requirements of AD 2004–12–07

(n) Accomplishing the actions specified in this AD terminates the requirements specified in paragraphs (b) and (c) of AD 2004–12–07.

Alternative Methods of Compliance (AMOCs)

(o)(1) The Manager, Seattle Aircraft Certification Office (ACO), FAA, has the authority to approve AMOCs for this AD, if requested in accordance with the procedures found in 14 CFR 39.19.

(2) To request a different method of compliance or a different compliance time for this AD, follow the procedures in 14 CFR 39.19. Before using any approved AMOC on any airplane to which the AMOC applies, notify your appropriate principal inspector (PI) in the FAA Flight Standards District Office (FSDO), or lacking a PI, your local FSDO.

(3) An AMOC that provides an acceptable level of safety may be used for any repair required by this AD, if it is approved by an Authorized Representative for the Boeing Commercial Airplanes Delegation Option Authorization Organization who has been authorized by the Manager, Seattle ACO, to make those findings. For a repair method to be approved, the repair must meet the certification basis of the airplane, and the approval must specifically refer to this AD.

(4) AMOCs approved previously in accordance with AD 2004–12–07 are approved as AMOCs for the corresponding provisions of this AD.

(5) AMOCs approved previously in accordance with AD 2005–12–04 are approved as AMOCs for the corresponding provisions of this AD.

Material Incorporated by Reference

(p) You must use Boeing Alert Service Bulletin 757–54A0047, Revision 3, dated June 27, 2007, to perform the actions that are required by this AD, unless the AD specifies otherwise. The Director of the Federal Register approved the incorporation by reference of this document in accordance with 5 U.S.C. 552(a) and 1 CFR part 51. Contact Boeing Commercial Airplanes, P.O. Box 3707, Seattle, Washington 98124–2207, for a copy of this service information. You may review copies at the FAA, Transport Airplane Directorate, 1601 Lind Avenue, SW., Renton, Washington; or at the National Archives and Records Administration (NARA). For information on the availability of this material at NARA, call 202–741–6030, or go to: *http://www.archives.gov/federal-register/cfr/ibr-locations.html.*

Issued in Renton, Washington, on July 31, 2007.

Ali Bahrami,

Manager, Transport Airplane Directorate, Aircraft Certification Service.

[FR Doc. E7–15419 Filed 8–8–07; 8:45 am]

BILLING CODE 4910–13–P

SECURITIES AND EXCHANGE COMMISSION

17 CFR Part 275

[Release No. IA–2628; File No. S7–25–06]

RIN 3235–AJ67

Prohibition of Fraud by Advisers to Certain Pooled Investment Vehicles

AGENCY: Securities and Exchange Commission.

ACTION: Final rule.

SUMMARY: The Securities and Exchange Commission is adopting a new rule that prohibits advisers to pooled investment vehicles from making false or misleading statements to, or otherwise defrauding, investors or prospective investors in those pooled vehicles. This rule is designed to clarify, in light of a recent court opinion, the Commission's ability to bring enforcement actions under the Investment Advisers Act of 1940 against investment advisers who defraud investors or prospective investors in a hedge fund or other pooled investment vehicle.

DATES: *Effective Date:* September 10, 2007.

FOR FURTHER INFORMATION CONTACT: David W. Blass, Assistant Director, Daniel S. Kahl, Branch Chief, or Vivien Liu, Senior Counsel, at 202–551–6787, Division of Investment Management, Securities and Exchange Commission, 100 F Street, NE., Washington, DC 20549–5041.

SUPPLEMENTARY INFORMATION: The Commission is adopting new rule 206(4)–8 under the Investment Advisers Act of 1940 (''Advisers Act'').[1]

I. Introduction

On December 13, 2006, we proposed a new rule under the Advisers Act that would prohibit advisers to pooled investment vehicles from defrauding investors or prospective investors in pooled investment vehicles they advise.[2] We proposed the rule in response to the opinion of the Court of Appeals for the District of Columbia Circuit in *Goldstein* v. *SEC,* which created some uncertainty regarding the application of sections 206(1) and 206(2) of the Advisers Act in certain cases where investors in a pool are defrauded by an investment adviser to that pool.[3] In addressing the scope of the exemption from registration in section 203(b)(3) of the Advisers Act and the meaning of ''client'' as used in that section, the Court of Appeals expressed the view that, for purposes of sections 206(1) and (2) of the Advisers Act, the ''client'' of an investment

[1] 15 U.S.C. 80b. Unless otherwise noted, when we refer to the Advisers Act, or any paragraph of the Advisers Act, we are referring to 15 U.S.C. 80b of the United States Code, at which the Advisers Act is codified.

[2] *Prohibition of Fraud by Advisers to Certain Pooled Investment Vehicles; Accredited Investors in Certain Private Investment Vehicles*, Investment Advisers Act Release No. 2576 (Dec. 27, 2006) [72 FR 400 (Jan. 4, 2007)] (the ''Proposing Release''). In the Proposing Release, we also proposed two new rules that would define the term ''accredited natural person'' under Regulation D and section 4(6) of the Securities Act of 1933 [15 U.S.C. 77d(6)] (''Securities Act''). As proposed, these rules would add to the existing definition of ''accredited investor'' and apply to private offerings of certain unregistered investment pools. On May 23, 2007, we voted to propose more general amendments to the definition of accredited investor. Proposed Modernization of Smaller Company Capital-Raising and Disclosure Requirements, Securities Act Release No. ____ (____, 2007) [72 FR ____ (____, 2007)]. We plan to defer consideration of our proposal to define the term accredited natural person until we have had the opportunity to evaluate fully the comments we received on that proposal together with those we receive on our May 2007 proposal.

[3] 451 F.3d 873 (D.C. Cir. 2006) (''Goldstein'').

adviser managing a pool is the pool itself, not an investor in the pool. As a result, it was unclear whether the Commission could continue to rely on sections 206(1) and (2) of the Advisers Act to bring enforcement actions in certain cases where investors in a pool are defrauded by an investment adviser to that pool.[4]

In its opinion, the Court of Appeals distinguished sections 206(1) and (2) from section 206(4) of the Advisers Act, which is not limited to conduct aimed at clients or prospective clients of investment advisers.[5] Section 206(4) provides us with rulemaking authority to define, and prescribe means reasonably designed to prevent, fraud by advisers.[6] We proposed rule 206(4)–8 under this authority.

We received 45 comment letters in response to our proposal.[7] Most commenters generally supported the proposal. Eighteen endorsed the rule as proposed, noting that the rule would strengthen the antifraud provisions of the Advisers Act or that the rule would clarify the Commission's enforcement authority with respect to advisers.[8] Others, however, urged that we make revisions that would restrict the scope of the rule to more narrowly define the conduct or acts it prohibits.[9]

Today, we are adopting new rule 206(4)–8 as proposed. The rule prohibits advisers from (i) making false or misleading statements to investors or prospective investors in hedge funds and other pooled investment vehicles they advise, or (ii) otherwise defrauding these investors. The rule clarifies that an adviser's duty to refrain from fraudulent conduct under the federal securities laws extends to the relationship with ultimate investors and that the Commission may bring enforcement actions under the Advisers Act against investment advisers who defraud investors or prospective investors in those pooled investment vehicles.

II. Discussion

Rule 206(4)–8 prohibits advisers to pooled investment vehicles from (i) making false or misleading statements to investors or prospective investors in those pools or (ii) otherwise defrauding those investors or prospective investors. We will enforce the rule through civil and administrative enforcement actions against advisers who violate it.

Section 206(4) authorizes the Commission to adopt rules and regulations that ''define, and prescribe means reasonably designed to prevent, such acts, practices, and courses of business as are fraudulent, deceptive, or manipulative.'' In adopting rule 206(4)–8, we intend to employ all of the broad authority that Congress provided us in section 206(4) and direct it at adviser conduct affecting an investor or potential investor in a pooled investment vehicle.

A. Scope of Rule 206(4)–8

Some commenters questioned the scope of the rule, arguing that the Commission should define fraud.[10] We believe that we have done so, only more broadly than some commenters would have us do. As the Proposing Release indicated, our intent is to prohibit all fraud on investors in pools managed by investment advisers. Congress expected that we would use the authority provided by section 206(4) to ''promulgate general antifraud rules capable of flexibility.''[11] The terms material false statements or omissions and ''acts, practices, and courses of business as are fraudulent, deceptive, or manipulative'' encompass the well-developed body of law under the antifraud provisions of the federal securities laws. The legal authorities identifying the types of acts, practices, and courses of business that are fraudulent, deceptive, or manipulative under the federal securities laws are numerous, and we believe that the conduct prohibited by rule 206(4)–8 is sufficiently clear and well understood.[12]

1. Investors and Prospective Investors

Rule 206(4)–8 prohibits investment advisers from making false or misleading statements to, or engaging in other fraud on, investors or prospective investors in a pooled investment vehicle they manage. The scope of the rule is modeled on that of sections 206(1) and (2) of the Advisers Act, which make unlawful fraud by advisers against clients or prospective clients. Rule 206(4)–8 prohibits false or misleading statements made, for example, to existing investors in account statements

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[4] Prior to the issuance of the *Goldstein* decision, we brought enforcement actions against advisers alleging false and misleading statements to investors under sections 206(1) and (2) of the Advisers Act. *See, e.g., SEC* v. *Kirk S. Wright, International Management Associates, LLC*, Litigation Release No. 19581 (Feb. 28, 2006); *SEC* v. *Wood River Capital Management, LLC*, Litigation Release No. 19428 (Oct. 13, 2005); *SEC* v. *Samuel Israel III; Daniel E. Marino; Bayou Management, LLC; Bayou Accredited Fund, LLC; Bayou Affiliates Fund, LLC; Bayou No Leverage Fund, LLC; and Bayou Superfund, LLC*, Litigation Release No. 19406 (Sept. 29, 2005); *SEC* v. *Beacon Hill Asset Management LLC*, Litigation Release No. 18745A (June 16, 2004).

[5] *See Goldstein, supra* note 3, at note 6. *See also United States* v. *Elliott*, 62 F.3d 1304, 1311 (11th Cir. 1995).

[6] Section 206(4) of the Advisers Act makes it unlawful for an investment adviser to ''engage in any act, practice, or course of business which is fraudulent, deceptive, or manipulative'' and authorizes us ''by rules and regulations [to] define, and prescribe means reasonably designed to prevent, such acts, practices, and courses of business as are fraudulent, deceptive, or manipulative.''

[7] We received over 600 comment letters that addressed the proposed amendments to the term ''accredited natural person'' under Regulation D and section 4(6) of the Securities Act. All of the public comments we received are available for inspection in our Public Reference Room at 100 F Street, NE., Washington DC, 20549 in File No. S7–25–06, or may be viewed at *http://www.sec.gov/comments/s7-25-06/s72506.shtml.*

[8] *E.g.*, Letter of the Alternative Investments Compliance Association (Mar. 5, 2007); Letter of the CFA Center for Financial Market Integrity (Mar. 9, 2007) (''CFA Center Letter''); Letter of the Coalition of Private Investment Companies (Mar. 9, 2007); Letter of the Commonwealth of Massachusetts (Mar. 9, 2007) (''Massachusetts Letter''); Letter of the Department of Banking of the State of Connecticut (Mar. 8, 2007); Letter of the North America Securities Administrators Association (Apr. 2, 2007) (''NASAA Letter''); and Letter of the U.S. Chamber of Commerce (Mar. 9, 2007). Another commenter observed that the proposed rules are broadly similar to current U.K. legislation and regulations. *See* Letter of Alternative Investment Management Association (Mar. 9, 2007) (''AIMA Letter'').

[9] *E.g.*, Letter of American Bar Association (Mar. 12, 2007) (''ABA Letter''); Letter of Davis Polk & Wardwell (Mar. 9, 2007) (''Davis Polk Letter''); Letter of Dechert LLP (Mar. 8, 2007) (''Dechert Letter''); Letter of New York City Bar (Mar. 8, 2007) (''NYCB Letter''); Letter of Schulte Roth & Zabel LLP (Mar. 9, 2007) (''Schulte Roth Letter''); and Letter of Sullivan & Cromwell LLP (Mar. 9, 2007) (''Sullivan & Cromwell Letter'').

[10] *E.g.*, ABA Letter, *supra* note 9; Letter of Debevoise & Plimpton LLP (Mar. 14, 2007); and NYCB Letter, *supra* note 9.

[11] S. Rep. No. 1760, 86th Cong., 2d. Sess. (June 28, 1960) at 4. *See* rule 206(4)–1(a)(5) [17 CFR. 275.206(4)–1(a)(5)] under the Advisers Act; rule 17j–1(b) [17 CFR 270.17j–1(b)] under the Investment Company Act of 1940 [15 U.S.C. 80a–1] (''Investment Company Act''); and rule 13e–3(b)(1) [17 CFR 240.13e–3(b)(1)] under the Securities Exchange Act of 1934 [15 U.S.C. 77a] (''Exchange Act'').

[12] Loss, Seligman, & Paredes, *Securities Regulation*, Chap. 9 (Fraud) (Fourth Ed. 2006); Hazen, *Treatise on The Law of Securities Regulation*, Vol. 3, Ch. 12 (Manipulation and Fraud—Civil Liability; Implied Private Remedies; SEC Rule 10b–5; Fraud in Connection With the Purchase or Sale of Securities; Improper Trading on Nonpublic Material Information) (Fifth Ed. 2005). *See, e.g.*, Superintendent of Insurance of New York v. *Bankers Life & Casualty Co.*, 404 U.S. 6, 11 n. 7 (1971) (''`We believe that section 10(b) and Rule 10b–5 prohibit all fraudulent schemes in connection with the purchase or sale of securities, whether the artifices employed involve a garden type variety of fraud, or present a unique form of deception. Novel or atypical methods should not provide immunity from the securities laws.' '' (quoting *A. T. Brod & Co.* v. *Perlow*, 375 F.2d 393, 397 (CA2 1967))); *Santa Fe Industries, Inc.* v. *Green*, 430 U.S. 462, 477 (1977) (''No doubt Congress meant to prohibit the full range of ingenious devices that might be used to manipulate securities prices.''). Moreover, the established legal principles are sufficiently flexible to encompass future novel factual scenarios. *United States* v. *Brown*, 555 F.2d 336, 339–40 (2d Cir. 1977) (''The fact that there is no litigated fact pattern precisely in point may constitute a tribute to the cupidity and ingenuity of the malefactors involved but hardly provides an escape from the penal sanctions of the securities fraud provisions here involved.'').

as well as to prospective investors in private placement memoranda, offering circulars, or responses to ''requests for proposals,'' electronic solicitations, and personal meetings arranged through capital introduction services.

Some commenters argued that the rule should not prohibit fraud against prospective investors in a pooled investment vehicle, asserting that such fraud does not actually harm investors until they, in fact, make an investment.[13] We disagree. False or misleading statements and other frauds by advisers are no less objectionable when made in an attempt to draw in new investors than when made to existing investors.[14] For similar policy reasons that we believe led Congress to apply the protections of sections 206(1) and (2) to prospective clients, we have decided to apply those of rule 206(4)–8 to prospective investors.[15] We believe that prohibiting false or misleading statements made to, or other fraud on, any prospective investors is a means reasonably designed to prevent fraud.

2. Unregistered Investment Advisers

Rule 206(4)–8 applies to both registered and unregistered investment advisers.[16] As we noted in the Proposing Release, many of our enforcement cases against advisers to pooled investment vehicles have been brought against advisers that are not registered under the Advisers Act, and we believe it is critical that we continue to be in a position to bring actions against unregistered advisers that manage pools and that defraud investors in those pools.[17] The two commenters that expressed an explicit view on this aspect of the proposal supported our application of the rule to advisers that are not registered with the Commission.[18]

3. Pooled Investment Vehicles

The rule we are adopting today applies to investment advisers with respect to any ''pooled investment vehicle'' they advise. The rule defines a pooled investment vehicle[19] as any investment company defined in section 3(a) of the Investment Company Act[20] and any privately offered pooled investment vehicle that is excluded from the definition of investment company by reason of either section 3(c)(1) or 3(c)(7) of the Investment Company Act.[21] As a result, the rule applies to advisers to hedge funds, private equity funds, venture capital funds, and other types of privately offered pools that invest in securities, as well as advisers to investment companies that are registered with us.[22]

Several commenters supported applying the protection of the new antifraud rule to investors in all these kinds of pooled investment vehicles, noting, for example, that every investor, not just the wealthy or sophisticated that typically invest in private pools, should be protected from fraud.[23] Some other commenters urged us not to apply the rule to advisers to registered investment companies, arguing that the rule is unnecessary because other provisions of the federal securities laws prohibiting fraud are available to the Commission to address these matters.[24] They expressed concern that application of another antifraud provision with different elements would be burdensome. These commenters claimed that the rule would, for example, make it necessary for advisers to conduct extensive reviews of all communications with clients. But the other antifraud provisions available to us contain different elements because they were not specifically designed to address frauds by investment advisers with respect to investors in pooled investment vehicles. In some cases, the other antifraud provisions may not permit us to proceed against the adviser.[25] As a result, the existing antifraud provisions may not be available to us in all cases. As we discussed above, before the *Goldstein* decision we had brought actions against advisers to mutual funds under sections 206(1) and (2) for defrauding investors in mutual funds.[26] Because, before the *Goldstein* decision, advisers to pooled investment vehicles operated with the understanding that the Advisers Act prohibited the conduct that this rule prohibits, we believe that advisers that are attentive to their traditional compliance responsibilities will not need to alter their business practices or take additional steps and incur new costs as a result of this rule's adoption.

B. Prohibition on False or Misleading Statements

Rule 206(4)–8(a)(1) prohibits any investment adviser to a pooled investment vehicle from making an untrue statement of a material fact to any investor or prospective investor in the pooled investment vehicle, or omitting to state a material fact necessary in order to make the statements made to any investor or

[13] Davis Polk Letter, *supra* note 9; Dechert Letter, *supra* note 9; NYCB Letter, *supra* note 9; Letter of the Securities Industry and Financial Markets Association (Mar. 9, 2007); Sullivan & Cromwell Letter, *supra* note 9.

[14] *See* CFA Center Letter, *supra* note 8.

[15] We have used the term ''prospective investor'' to give the term similar scope to the term ''prospective client'' in sections 206(1) and (2). *See, e.g., In the Matter of Ralph Harold Seipel*, 38 S.E.C. 256, 257–58 (1958) (the solicitation of clients is part of the activity of an investment adviser and it is immaterial for purposes of an enforcement action under sections 206(1) and (2) that an adviser engaging in fraudulent solicitations was not successful in his efforts to obtain clients).

[16] A few commenters requested that we clarify how we intend to apply rule 206(4)–8 to offshore advisers' interaction with non-U.S. investors. *See* AIMA Letter, *supra* note 8; Letter of Jones Day (Mar. 9, 2007); Sullivan & Cromwell Letter, *supra* note 9. Our adoption of this rule will not alter our jurisdictional authority.

[17] Proposing Release, *supra* note 2, at note 14.

[18] Massachusetts Letter, *supra* note 8; NASAA Letter, *supra* note 8.

[19] Rule 206(4)–8(b).

[20] 15 U.S.C. 80a–3(a). Unless otherwise noted, when we refer to the Investment Company Act, or any paragraph of the Investment Company Act, we are referring to 15 U.S.C. 80a of the United States Code, at which the Company Act is codified.

[21] Section 3(c)(1) of the Investment Company Act excludes from the definition of investment company an issuer the securities (other than short-term paper) of which are beneficially owned by not more than 100 persons and that is not making or proposing to make a public offering of its securities. Section 3(c)(7) of the Investment Company Act excludes from the definition of investment company an issuer the outstanding securities of which are owned exclusively by persons who, at the time of acquisition of such securities, are ''qualified purchasers'' and that is not making or proposing to make a public offering of its securities. ''Qualified purchaser'' is defined in section 2(a)(51) of the Investment Company Act generally to include a natural person (or a company owned by two or more related natural persons) who owns not less than $5,000,000 in investments; a person, acting for its own account or accounts of other qualified purchasers, who owns and invests on a discretionary basis, not less than $25,000,000; and a trust whose trustee, and each of its settlors, is a qualified purchaser.

[22] We have brought enforcement actions under the Advisers Act against advisers to these types of funds. *See, e.g., In the Matter of Askin Capital Management, L.P and David J. Askin*, Investment Advisers Act Release No. 1492 (May 23, 1995) (hedge fund); *In the Matter of Thayer Capital Partners*, Investment Advisers Act Release No. 2276 (Aug. 12, 2004) (private equity fund); *SEC* v. *Michael A. Liberty*, Litigation Release No. 19601 (Mar. 8, 2006) (venture capital fund).

[23] *E.g.*, NASAA Letter, *supra* note 8.

[24] *E.g.*, ABA Letter, *supra* note 9; Letter of Investment Adviser Association (Mar. 9, 2007); Letter of Investment Company Institute (Mar. 9, 2007) (''ICI Letter''); Sullivan & Cromwell Letter, *supra* note 9. Commenters noted in particular that section 34(b) of the Investment Company Act already prohibits an adviser from making fraudulent material statements or omissions in a fund's registration statement or in required records.

[25] This may be the case with respect to section 34(b) of the Investment Company Act, for example, if the adviser's fraudulent statements are not made in a document described in that section, or with respect to rule 10b–5 under the Exchange Act, where the fraudulent conduct does not relate to a misstatement or omission in connection with the purchase or sale of any security.

[26] *See, e.g., In the Matter of Van Kampen Investment Advisory Corp.*, Investment Advisers Act Release No. 1819 (Sept. 8, 1999); *In the Matter of The Dreyfus Corporation*, Investment Advisers Act Release No. 1870 (May 10, 2000); *In the Matter of Federated Investment Management Company*, Investment Advisers Act Release No. 2448 (Nov. 28, 2005).

prospective investor in the pooled investment vehicle, in the light of the circumstances under which they were made, not misleading.[27]

The provision is very similar to those in many of our antifraud laws and rules that, depending upon the circumstances, may also be applicable to the same investor communications.[28] Sections 206(1) and (2) have imposed similar obligations on advisers since 1940 and, before *Goldstein*, were commonly accepted as imposing similar requirements on communications with investors in a fund. For these reasons, and because the nature of the duty to communicate without false statements is so well developed in current law, we believe that commenters' concerns about the breadth of the prohibition or any chilling effect the new rule might have on investor communications are misplaced.[29] Advisers to pooled investment vehicles attentive to their traditional compliance responsibilities will not need to alter their communications with investors.

Rule 206(4)–8(a)(1) prohibits advisers to pooled investment vehicles from making any materially false or misleading statements to investors in the pool regardless of whether the pool is offering, selling, or redeeming securities. While the new rule differs in this aspect from rule 10b–5 under the Exchange Act, the conduct prohibited is similar. The new rule prohibits, for example, materially false or misleading statements regarding investment strategies the pooled investment vehicle will pursue, the experience and credentials of the adviser (or its associated persons), the risks associated with an investment in the pool, the performance of the pool or other funds advised by the adviser, the valuation of the pool or investor accounts in it, and practices the adviser follows in the operation of its advisory business such as how the adviser allocates investment opportunities.[30]

C. Prohibition of Other Frauds

Rule 206(4)–8(a)(2) makes it a fraudulent, deceptive, or manipulative act, practice, or course of business for any investment adviser to a pooled investment vehicle to ''otherwise engage in any act, practice, or course of business that is fraudulent, deceptive, or manipulative with respect to any investor or prospective investor in the pooled investment vehicle.'' [31] As we noted in the Proposing Release, the wording of this provision is drawn from the first sentence of section 206(4) and is designed to apply more broadly to deceptive conduct that may not involve statements.[32]

Some commenters asserted that section 206(4) provides us authority only to adopt prophylactic rules that explicitly identify conduct that would be fraudulent under the new rule.[33] We believe our authority is broader. We do not believe that the commenters' suggested approach would be consistent with the purposes of the Advisers Act or the protection of investors. That approach would have us adopt the rule prohibiting fraudulent communications but not fraudulent conduct.[34] But, section 206(4) itself specifically authorizes us to adopt rules defining and prescribing ''acts, practices and courses of business,'' (*i.e.*, conduct), and does not explicitly refer to communications, which, nonetheless, represent a form of an act, practice, or course of business. In addition, rule 206(4)–8 as adopted would provide greater protection to investors in pooled investment vehicles.

Alternatively, commenters would have us adopt a rule prohibiting identified known fraudulent conduct or would have us provide detailed commentary describing specific forms of fraudulent conduct that the rule would prohibit.[35] Either approach would fail to prohibit fraudulent conduct we did not identify, and could provide a roadmap for those wishing to engage in fraudulent conduct. This approach would be inconsistent with our historical application of the federal securities laws under which broad prohibitions have been applied against specific harmful activity.

D. Other Matters

We noted in the Proposing Release that, unlike violations of rule 10b–5 under the Exchange Act, the Commission would not need to demonstrate that an adviser violating rule 206(4)–8 acted with scienter.[36] Commenters questioned whether the rule should encompass negligent conduct, arguing that it would ''expand the concept of fraud itself beyond its original meaning.'' [37] We read the language of section 206(4) as not by its terms limited to knowing or deliberate conduct. For example, section 206(4) encompasses ''acts, practices, and courses of business as are * * * deceptive,'' thereby reaching conduct that is negligently deceptive as well as conduct that is recklessly or deliberately deceptive. In addition, the Court of Appeals for the District of Columbia Circuit concluded that ''scienter is not required under section 206(4).'' [38] We believe use of a negligence standard also is appropriate as a method reasonably designed to prevent fraud. As the Supreme Court noted in *U.S.* v. *O'Hagan*, ''[a] prophylactic measure, because its mission is to prevent, typically encompasses more than the core activity prohibited.'' [39] In *O'Hagan*, the Court held that under section 14(e) ''the Commission may prohibit acts, not themselves fraudulent under the common law or § 10(b), if the prohibition is 'reasonably designed to prevent * * * acts and practices [that] are fraudulent.' '' [40] Along these lines, the prohibitions in rule 206(4)–8 are reasonably designed to prevent fraud. We believe that, by taking sufficient care to avoid negligent conduct, advisers will be more likely to avoid reckless deception. Since the Commission clearly is authorized to prescribe

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[27] A fact is material if there is a substantial likelihood that a reasonable investor in making an investment decision would consider it as having significantly altered the total mix of information available. *Basic, Inc.* v. *Levinson*, 485 U.S. 224, 231–32 (1988); *TSC Industries, Inc.* v. *Northway, Inc.*, 426 U.S. 438, 449 (1976). *See also In the Matter of Van Kampen Investment Advisory Corp., supra* note 26; *In the Matter of the Dreyfus Corporation, supra* note 26.

[28] *See, e.g.*, sections 12 and 17 of the Securities Act [15 U.S.C. 77l, 77q]; section 14 of the Exchange Act [15 U.S.C. 78n]; section 34 of the Investment Company Act; rules 156, 159, and 610 under the Securities Act [17 CFR 230.156, 230.159, 230.610]; rules 10b–5, 13e–3, 13e–4, and 15c1–2 under the Exchange Act [17 CFR 240.10b–5, 240.13e–3, 240.13e–4, 240.15c1–2]; and rule 17j–1 under the Investment Company Act [17 CFR 270.17j–1]).

[29] Letter of Managed Funds Association (Mar. 9, 2007) (''MFA Letter''); NYCB Letter, *supra* note 9; Davis Polk Letter, *supra* note 9; Dechert Letter, *supra* note 9; Letter of Seward & Kissel LLP (Mar. 8, 2007) (''Seward & Kissel Letter'').

[30] We have previously brought enforcement actions alleging these or similar types of frauds. *See* Proposing Release, *supra* note 2, at note 29.

[31] Rule 206(4)–8(a)(2).

[32] *See* Section II.C of the Proposing Release, *supra* note 2.

[33] ABA Letter, *supra* note 9; ICI Letter, *supra* note 24; Schulte Roth Letter, *supra* note 9; Sullivan & Cromwell Letter, *supra* note 9.

[34] *See, e.g.*, ABA Letter, *supra* note 9.

[35] *Id.*

[36] Section II.B of the Proposing Release, *supra* note 2.

[37] *See* ABA Letter, *supra* note 9 at page 3.

[38] *SEC* v. *Steadman*, 967 F.2d 636, at 647 (D.C. Cir. 1992). The court in *Steadman* analogized section 206(4) of the Advisers Act to section 17(a)(3) of the Securities Act, which the Supreme Court had held did not require a finding of scienter, *id.* (citing *Aaron* v. *SEC*, 446 U.S. 680 (1980)). In discussing section 17(a)(3) and its lack of a scienter requirement, the *Steadman* court observed that, similarly, a violation of section 206(2) of the Advisers Act could rest on a finding of simple negligence. *Id.* at 643, note 5. *But see Aaron* at 690–91 (citing *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 199 (1976)); *cf.* S. Rep. No. 1760, 86th Cong., 2d. Sess. (June 28, 1960) at 8 and H. R. Rep. 2179, 86th Cong., 2d Sess. (Aug. 26, 1960) at 8 (comparing section 206(4) to section 15(c)(2) of the Exchange Act).

[39] *U.S.* v. *O'Hagan*, 521 U.S. 642, 672–73 (1997).

[40] *Id.* at 673.

conduct that goes beyond fraud as a means reasonably designed to prevent fraud, prohibiting deceptive conduct done negligently is a way to accomplish this objective.

Rule 206(4)–8 does not create under the Advisers Act a fiduciary duty to investors or prospective investors in a pooled investment vehicle not otherwise imposed by law. Nor does the rule alter any duty or obligation an adviser has under the Advisers Act, any other federal law or regulation, or any state law or regulation (including state securities laws) to investors in a pooled investment vehicle it advises.[41] The rule, for example, will permit us to bring an enforcement action against an investment adviser that violates a fiduciary duty imposed by other law if the violation of such law or obligation also constitutes an act, practice, or course of business that is fraudulent, deceptive, or manipulative within the meaning of the rule and section 206(4).[42]

Finally, the rule does not create a private right of action.[43]

III. Paperwork Reduction Act

The Paperwork Reduction Act of 1995 does not apply because rule 206(4)–8 does not impose a new ''collection of information'' within the meaning of the Paperwork Reduction Act of 1995. The rule does not create any filing, reporting, recordkeeping, or disclosure requirements for investment advisers subject to the rule. Accordingly, there is no ''collection of information'' under the Paperwork Reduction Act that requires the approval of the Office of Management and Budget under 44 U.S.C. 3501.

IV. Cost-Benefit Analysis

The Commission is sensitive to costs imposed by our rules and the benefits that derive from them. In the Proposing Release, we encouraged commenters to discuss any potential costs and benefits that we did not consider in our discussion. Three commenters addressed the issue of cost. Two of them stated their belief that the rule would increase advisers' costs of compliance, by, for example, making it necessary for advisers to conduct extensive reviews of all communications with clients.[44] One stated that the rule would achieve a reasonable balance of providing important benefits to investors at an acceptable cost.[45] None of the three commenters, however, provided analysis or empirical data in connection with their statements.

The rule makes it a fraudulent, deceptive, or manipulative act, practice, or course of business within the meaning of section 206(4) for any investment adviser to a pooled investment vehicle to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, to any investor or prospective investor in the pooled investment vehicle. The rule also makes it a fraudulent, deceptive, or manipulative act, practice, or course of business within the meaning of section 206(4) for any investment adviser to a pooled investment vehicle to otherwise engage in any act, practice, or course of business that is fraudulent, deceptive, or manipulative with respect to any investor or prospective investor in the pooled investment vehicle. For the reasons discussed, we do not believe that the rule will require advisers to incur new or additional costs.

Investment advisers to pooled investment vehicles should not be making untrue statements or omitting material facts or otherwise be engaged in fraud with respect to investors or prospective investors in pooled investment vehicles today, because federal authorities, state authorities, and private litigants often can, and do, seek redress from the adviser for the untrue statements or omissions or other frauds. In most cases, the conduct that the rule prohibits is already prohibited by federal securities statutes,[46] other federal statutes (including federal wire fraud statutes),[47] as well as state law.[48]

We recognize that there are costs involved in assuring that communications to investors and prospective investors do not contain untrue or misleading statements and preventing other frauds. Advisers have incurred, and will continue to incur, these costs due to the prohibitions and deterrent effect of the law and rules that apply under these circumstances. While each of the provisions noted above may have different limitation periods, apply in different factual circumstances, or require the government (or a private litigant) to prove different states of mind than the rule, as discussed above we believe that the multiple prohibitions against fraud, and the consequences under both criminal and civil law for fraud, should currently cause an adviser to take the precautions it deems necessary to refrain from such conduct.

Furthermore, prior to *Goldstein*, advisers operated with the understanding that the Advisers Act prohibited the same conduct that would be prohibited by the rule. Accordingly, we do not believe that advisers to pooled investment vehicles attentive to their traditional compliance responsibilities will need to take steps or alter their business practices in such a way that will require them to incur new or additional costs as a result of the adoption of the rule.

We also recognize that the rule may cause some advisers to pay more attention to the information they present to better guard against making an untrue or misleading statement to an investor or prospective investor and to reevaluate measures that are intended to prevent fraud. As a consequence, some advisers might seek guidance, legal or otherwise, and more closely review the

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[41] For example, under the Uniform Limited Partnership Act, advisers who serve as general partners owe fiduciary duties to the limited partners. Unif. Limited Partnership Act section 408 (2001).

[42] For example, if an adviser has a duty from a source other than the rule to make a material disclosure to an investor in a fund and negligently or deliberately fails to make the disclosure, the rule would apply to the failure.

[43] The Supreme Court has held that ''there exists a limited private remedy under the Investment Advisers Act of 1940 to void an investment adviser's contract, but that the Act confers no other private causes of action, legal or equitable.'' *Transamerica Mortgage Advisors, Inc.* v. *Lewis*, 444 U.S. 11 at 24 (1979) (footnote omitted).

[44] NYCB Letter, *supra* note 9; Seward & Kissel Letter, *supra* note 29.

[45] CFA Center Letter, *supra* note 8.

[46] *See, e.g.*, section 10(b) of the Exchange Act [15 U.S.C. 78j(b)] and section 17(a) of the Securities Act [15 U.S.C. 77q] which would apply when the false statements are made ''in connection with the purchase or sale of a security'' or involve the ''offer or sale'' of a security, and section 34(b) of the Investment Company Act which makes it unlawful ''to make any untrue statement of a material fact in any registration statement, application, report, account, record, or other document filed or transmitted pursuant to [the Investment Company Act] * * *.''

[47] *See, e.g.*, 18 U.S.C. 1341 (Frauds and Swindles) and 18 U.S.C. 1343 (Fraud by wire, radio, or television) which make it a criminal offense to use the mails or to communicate by means of wire, having devised a scheme to defraud or for obtaining money or property by means of false or fraudulent pretenses, and 18 U.S.C. 1957 (Engaging in monetary transactions in property derived from specified unlawful activity) which makes it a criminal racketeering offense to engage or attempt to engage in a transaction in criminally derived property of a value greater than $10,000.

[48] *See, e.g., Metro Communications Corp. BVI* v. *Advanced Mobilecomm Technologies*, 854 A.2d 121, 156 (Del. Ch. 2004) (court held that plaintiff-former member of LLC had sufficiently alleged a common law fraud claim based on the allegation that a series of reports by LLC's managers contained misleading statements; court stated that ''[i]n the usual fraud case, the speaking party who is subject to an accusation of fraud is on the opposite side of a commercial transaction from the plaintiff, who alleges that but for the material misstatements or omissions of the speaking party he would not have contracted with the speaking party'').

information that they disseminate to investors and prospective investors and the antifraud related policies and procedures they have implemented. While increased concern about making false statements or committing fraud could be attributable to the new rule, advisers should already be incurring these costs to ensure truthfulness and prevent fraud, regardless of the rule, because of the myriad of laws or regulations that may already apply.

The principal benefit of the rule is that it clearly enables the Commission to bring enforcement actions under the Advisers Act, if an adviser to a pooled investment vehicle disseminates false or misleading information to investors or prospective investors or otherwise commits fraud with respect to any investor or prospective investor. As noted above, the existing antifraud provisions may not be available to us in all cases. Through our enforcement actions we are able to protect fund investor assets by stopping ongoing frauds,[49] barring persons that have committed certain specified violations or offenses from being associated with an investment adviser,[50] imposing penalties,[51] seeking court orders to protect fund assets,[52] and to order disgorgement of ill-gotten gains.[53] Moreover, we believe that rule 206(4)–8 will deter advisers to pooled investment vehicles from engaging in fraudulent conduct with respect to investors in those pools and will provide investors with greater confidence when investing in pooled investment vehicles.

V. Regulatory Flexibility Act Analysis

The Commission certified, pursuant to section 605(b) of the Regulatory Flexibility Act, that rule 206(4)–8 will not have a significant economic impact on a substantial number of small entities.[54] This certification was included in the Proposing Release.[55] While we encouraged written comment regarding this certification, none of the commenters responded to this request.

[49] *See* section 203(k) of the Advisers Act (Commission authority to issue cease and desist orders).

[50] *See* section 203(f) of the Advisers Act (Commission authority to bar a person from being associated with an investment adviser).

[51] *See* section 203(i) of the Advisers Act (Commission authority to impose civil penalties).

[52] *See* section 209(d) of the Advisers Act (Commission authority to seek injunctions and restraining orders in federal court).

[53] *See* section 203(j) of the Advisers Act (Commission authority to order disgorgement).

[54] 5 U.S.C. 605(b).

[55] Section VII.A of the Proposing Release, *supra* note 2.

VI. Statutory Authority

We are adopting new rule 206(4)–8 pursuant to our authority set forth in sections 206(4) and 211(a) of the Advisers Act (15 U.S.C. 80b–6(4) and 80b–11(a)).

List of Subjects in 17 CFR Part 275

Reporting and recordkeeping requirements, Securities.

VII. Text of Rules

■ For the reasons set out in the preamble, Title 17, Chapter II of the Code of Federal Regulations is amended as follows:

PART 275—RULES AND REGULATIONS, INVESTMENT ADVISERS ACT OF 1940

■ 1. The authority citation for Part 275 continues to read in part as follows:

Authority: 15 U.S.C. 80b–2(a)(11)(F), 80b–2(a)(17), 80b–3, 80b–4, 80b–4a, 80b–6(4), 80b–6a, and 80b–11, unless otherwise noted.

* * * * *

■ 2. Section 275.206(4)–8 is added to read as follows:

§ 206(4)–8 Pooled investment vehicles.

(a) *Prohibition.* It shall constitute a fraudulent, deceptive, or manipulative act, practice, or course of business within the meaning of section 206(4) of the Act (15 U.S.C. 80b–6(4)) for any investment adviser to a pooled investment vehicle to:

(1) Make any untrue statement of a material fact or to omit to state a material fact necessary to make the statements made, in the light of the circumstances under which they were made, not misleading, to any investor or prospective investor in the pooled investment vehicle; or

(2) Otherwise engage in any act, practice, or course of business that is fraudulent, deceptive, or manipulative with respect to any investor or prospective investor in the pooled investment vehicle.

(b) *Definition.* For purposes of this section ''pooled investment vehicle'' means any investment company as defined in section 3(a) of the Investment Company Act of 1940 (15 U.S.C. 80a–3(a)) or any company that would be an investment company under section 3(a) of that Act but for the exclusion provided from that definition by either section 3(c)(1) or section 3(c)(7) of that Act (15 U.S.C. 80a–3(c)(1) or (7)).

Dated: August 3, 2007.

By the Commission.

Nancy M. Morris,

Secretary.

Concurrence of Commissioner Paul S. Atkins to the Prohibition of Fraud by Advisers to Certain Pooled Investment Vehicles

New Rule 206(4)–8 under the Investment Advisers Act of 1940 (''Advisers Act''),[56] which we adopt today, prohibits advisors from (i) making false or misleading statements to investors or prospective investors in hedge funds and other pooled investment vehicles they advise, or (ii) otherwise defrauding these investors.[57] Although the SEC has other ways to reach fraud by advisors, this new rule will fill in gaps in the coverage of other transaction-based, anti-fraud provisions so that the SEC may pursue advisors of pooled investment vehicles who have defrauded investors and prospective investors in the course of their acting as fund advisors. I support the new rule, but I am writing separately to express my disagreement with the conclusions in the Adopting Release[58] related to the requisite mental state for violation of the rule.[59]

In discussing the mental state required for violation of the rule, the Adopting Release states that ''the Commission would not need to demonstrate that an adviser violating rule 206(4)–8 acted with scienter.''[60]

[56] 15 U.S.C. 80b.

[57] 17 CFR 275.206(4)–8. Paragraph (a) of the new rule provides:

Prohibition. It shall constitute a fraudulent, deceptive, or manipulative act, practice or course of business within the meaning of section 206(4) of the Act (15 U.S.C. 80b–6(4)) for any investment adviser to a pooled investment vehicle to:

(1) Make any untrue statement of a material fact or to omit to state a material fact necessary to make the statements made, in the light of the circumstances under which they were made, not misleading, to any investor or prospective investor in the pooled investment vehicle; or

(2) Otherwise engage in any act, practice, or course of business that is fraudulent, deceptive, or manipulative with respect to any investor or prospective investor in the pooled investment vehicle.

Paragraph (b) of the rule defines a ''pooled investment vehicle'' to include any investment company and any company that relies on an exclusion from the definition of ''investment company'' in Section (3)(c)(1) or (3)(c)(7) of the Investment Company Act [15 U.S.C. 80a–3(c)(1) or (7))].

[58] Prohibition of Fraud by Advisers to Certain Pooled Investment Vehicles, Advisers Act Release No. 2628 (Aug. 3, 2007) (''Adopting Release'').

[59] *See* Section II.D of the Adopting Release. I agree with the Section's conclusions with respect to fiduciary duty (Rule 206(4)–8 does not create a fiduciary duty) and private rights of action (Rule 206(4)–8 does not create any private rights of action).

[60] Adopting Release, at text accompanying note 36.

According to the Adopting Release, therefore, the rule covers negligent conduct as well as intentional conduct. My objections to this interpretation of the rule's scope are twofold. First, I do not believe that a negligence standard is consistent with the Commission's authority under Section 206(4). Second, even if a negligence standard were within our authority, for policy reasons, we should require a finding of scienter [61] as part of establishing a violation under this anti-fraud rule.

The Adopting Release offers several arguments in support of a negligence standard. First, it argues that the language of section 206(4) is not limited to knowing or deliberate conduct. In support of this argument, it cites the decision by the United States Court of Appeals for the District of Columbia Circuit in *SEC* v. *Steadman*.[62] Second, the Adopting Release contends that use of a negligence standard is an appropriate method reasonably designed to prevent fraud. In support of this contention, it cites *U.S.* v. *O'Hagan*.[63] I will discuss each of these in turn.

The language of Section 206(4) does not reach negligent conduct. Section 206(4) makes it unlawful for an advisor ''to engage in any act, practice, or course of business which is fraudulent, deceptive, or manipulative'' and directs the Commission ''by rules and regulations [to] define, and prescribe means reasonably designed to prevent, such acts, practices, and courses of business as are fraudulent, deceptive, or manipulative.''

The Adopting Release maintains that, because Section 206(4) ''encompasses 'acts, practices, and courses of business as are * * * deceptive,' '' it reaches ''conduct that is negligently deceptive as well as conduct that is recklessly or deliberately deceptive.'' [64] As the Supreme Court has said, however, ''it is a 'familiar principle of statutory construction that words grouped in a list should be given related meaning.' '' [65] Hence, it is inappropriate to base a conclusion that negligent conduct is reached by looking at the term ''deceptive'' apart from its companion terms.

In the Section 10(b) context, the Supreme Court has accorded special significance to the term ''manipulative'':

> Use of the word ''manipulative'' is especially significant. It is and was virtually a term of art when used in connection with securities markets. It connotes intentional or willful conduct designed to deceive or defraud investors by controlling or artificially affecting the price of securities.[66]

The language of Section 206(4), like the language of Section 10(b), would seem then to suggest a scienter requirement.

The Adopting Release, however, cites for the contrary conclusion a decision by the United States Court of Appeals for the District of Columbia. Indeed, it is true that in *SEC* v. *Steadman*, the court held that ''scienter is not required under section 206(4).'' [67] The court reached its conclusion by comparing the language of Section 206(4) to the language of Section 17(a)(3) under the Securities Act of 1933,[68] which makes it unlawful ''to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.'' [69] The *Steadman* court drew a comparison between Section 17(a)(3)'s ''transaction, practice, or course of business'' and Section 206(4)'s ''act, practice, or course of business.'' The court, relying on the Supreme Court's decision in *Aaron*, held that, in both cases, the focus was on effect. [70] The Supreme Court in *Aaron*, however, placed considerable weight on the terms ''operate'' or ''would operate,'' neither of which appears in Section 206(4).[71] In fact, Section 206(4) instead uses the affirmative word ''is,'' which would seem to de-emphasize effect.[72] Further, while Section 17(a)(3) speaks of only ''fraud'' and ''deceit,'' Section 206(4) also includes ''manipulative.''

It is also helpful to note that Section 206(4), which was adopted in 1960,[73] was modeled on Section 15(c)(2) under the Securities Exchange Act of 1934.[74] Section 15(c)(2) makes it unlawful for brokers and dealers to effect transactions in or induce the purchase or sale of securities in connection with which they ''engage[] in any fraudulent, deceptive, or manipulative act or practices, or make[] any fictitious quotation.'' [75] Hence, as the legislative history of Section 206(4) noted, Section 206(4) ''is comparable to section 15(c)(2).'' [76] The *Steadman* opinion did not address the link between Sections 206(4) and 15(c)(2).

Section 14(e) under the Exchange Act, which relates to tender offers, also follows the Section 15(c)(2) pattern.[77] Section 14(e), like Section 206(4), includes both a proscription against ''engag[ing] in any fraudulent, deceptive, or manipulative acts or practices'' and a directive that the SEC ''by rules and regulations define, and prescribe means reasonably designed to prevent such acts and practices as are fraudulent, deceptive, or manipulative.'' Because of the similarities, it is useful to look at the Supreme Court's interpretation of Section 14(e). In *Schreiber* v. *Burlington Northern,* the Supreme Court relied on *Hochfelder's* interpretation of the term ''manipulative'' in the Section 10(b) context to interpret that term in the Section 14(e) context.[78] The *Schreiber Court* noted that the addition of the rulemaking authorization to Section 14(e) did not ''suggest[] any change in the meaning of 'manipulative' itself.'' [79] In *U.S.* v. *O'Hagan,* The Supreme Court again looked at Section 14(e). This time, it considered whether Rule 14e–3(a), which prohibits trading on undisclosed information in connection with a tender offer, exceeds the SEC's authority under Section 14(e) given that the prohibition applies regardless of whether there is a duty to disclose. The Court held that

[61] ''Scienter'' is ''a mental state embracing intent to deceive, manipulate, or defraud.'' *Ernst & Ernst* v. *Hochfelder,* 425 U.S. 185, 194 (1976). Recklessness has also been found to satisfy a scienter standard.

[62] *SEC* v. *Steadman,* 967 F.2d 636 (D.C. Cir. 1992).

[63] *U.S.* v. *O'Hagan,* 521 U.S. 642, 672–73 (1997).

[64] Adopting Release at Section II.D.

[65] *Schreiber* v. *Burlington Northern, Inc.* 472 U.S. 1, 8 (1985) (quoting *Securities Industry Assn.* v. *Board of Governors, FRS,* 468 U.S. 207, 218 (1984).

[66] *Hochfelder,* 425 U.S. at 199 (footnote to dictionary definition omitted). *Hochfelder* considered whether scienter was a necessary component of a private action under Section 10(b). In a subsequent case, the Court considered whether scienter was a necessary element of an injunctive action by the SEC and concluded that it was. *Aaron* v. *SEC,* 446 U.S. 680, 691 (1980) (''the rationale of *Hochfelder* ineluctably leads to the conclusion that scienter is an element of a violation of section 10(b) and Rule 10b–5, regardless of the identity of the plaintiff or the nature of the relief sought.'').

[67] *Steadman,* 967 F.2d at 647.

[68] 15 U.S.C. 77a *et seq.*

[69] 15 U.S.C. 77q(a)(3).

[70] *Steadman* at 647.

[71] *Aaron,* 446 U.S. at 696–97 (''the language of section 17(a)(3), under which it is unlawful for any person to 'engage in any transaction, practice, or course of business which *operates* or *would operate* as a fraud or deceit,' quite plainly focuses upon the *effect* of particular conduct * * * rather than upon the culpability of the person responsible.'') (emphasis in original).

[72] Section 206(4) makes it unlawful ''to engage in any act, practice, or course of business which *is* fraudulent, deceptive, or manipulative.'' (Emphasis added.)

[73] S. Rep. No. 86–1760, at 4 (1960) (''The proposal has precedent in similar authority granted to the SEC over brokers and dealers by the Securities Exchange Act of 1934.'').

[74] 15 U.S.C. 78a *et seq.*

[75] 15 U.S.C. 78o(c)(2).

[76] H.R. Rep. No. 86–2179, at 8 (1960). *See also* S. Rep. No. 86–1760, at 8 (1960) (''almost the identical wording of section 15(c)(2)'').

[77] 15 U.S.C. 78n(e).

[78] *Schreiber,* 472 U.S. at 12 (''We hold that the term, 'manipulative' as used in § 14(e) requires misrepresentation or nondisclosure. It connotes 'conduct designed to deceive or defraud investors by controlling or artificially affecting the price of securities.'') (citing *Hochfelder,* 425 U.S. at 199).

[79] *Id.* at 12 n.11.

Rule 14e–3(a) was within the SEC's authority under Section 14(e) because Section 14(e) allows the SEC to ''prohibit acts, not themselves fraudulent under the common law or § 10(b), if the prohibition is 'reasonably designed to prevent * * * acts and practices [that] are fraudulent.' '' [80] The lesson from both of these cases is that the SEC cannot effect a change in the meaning of specific statutory terms under its comparable Section 206(4) rulemaking authority.

The Adopting Release asserts that, under *O'Hagan,* a negligence standard is a means reasonably designed to prevent fraud. As the Adopting Release notes, conduct outside of the bounds of the statutory prohibition can be prohibited by Commission rule under Section 206(4). The rule that we are adopting here, however, differs markedly from the rules at issue in *O'Hagan* and *Steadman*.[81] Both of those rules were narrowly targeted rules that covered clearly-defined behavior. They were designed to prohibit conduct, that, although outside of the ''core activity prohibited'' by the statute, were designed to ''assure the efficacy'' of the statute.[82]

Rule 206(4)–8(a)(2), by contrast, is as broad as the statute itself. It essentially repeats the statutory prohibition. It does not logically follow, therefore, that lowering the standard of care would be the type of ''means reasonably designed to prevent'' within the contemplation of the regulatory mandate within Section 206(4). Lowering the standard of care is instead an attempt to rewrite the statute by assigning new definitions to the words of the statute. A potential unfortunate consequence of the Adopting Release's change in mental state is that it is now arguably contrary to statute and therefore might interfere with the SEC's ability to use the rule effectively.[83] Congress included a rulemaking directive in order to give the SEC the necessary authority to provide clarity in this area about the types of practices covered by the statute's broad prohibition,[84] not to alter the standard of care that Congress selected through the language it used.[85] Imposing a negligence standard is particularly improper given that, as the Adopting Release notes, ''Rule 206(4)–8 does not create under the Advisers Act a fiduciary duty to investors and prospective investors in a pooled investment vehicle.'' [86]

Finally, from a purely practical perspective, I dispute the regulatory approach underlying the contention that ''by taking sufficient care to avoid negligent conduct, advisers will be more likely to avoid reckless deception.'' [87] By an extension of that same logic, a strict liability standard would evoke even more care by advisors. Even if the SEC is authorized to pick the standard of care that applies broadly to all ''fraudulent, deceptive, or manipulative'' acts and practices, arbitrarily selecting a higher standard of care ''just to be on the safe side'' has the potential of misdirecting enforcement and inspection resources and chilling well-intentioned advisors from serving their investors.

[FR Doc. E7–15531 Filed 8–8–07; 8:45 am]

BILLING CODE 8010–01–P

SOCIAL SECURITY ADMINISTRATION

20 CFR Parts 404 and 416

[Docket No. SSA 2007–0036]

RIN 0960–AG49

Amendment to the Attorney Advisor Program

AGENCY: Social Security Administration.

ACTION: Interim final rule with request for comments.

SUMMARY: We are announcing this interim final rule to modify, on a temporary basis, the prehearing procedures we follow in claims for Social Security disability benefits or supplemental security income (SSI) payments based on disability or blindness. Under the interim final rule, we may allow certain attorney advisors, under managerial oversight, to conduct certain prehearing proceedings, and where the documentary record developed as a result of these proceedings warrants, issue decisions that are wholly favorable to the parties to the hearing.

DATES: *Effective date:* This rule is effective August 9, 2007. *Comment date:* To be sure that your comments are considered, we must receive them no later than October 9, 2007.

ADDRESSES: You may give us your comments by: Internet through the Federal eRulemaking Portal at *http://www.regulations.gov*; e-mail to *regulations@ssa.gov*; telefax to (410) 966–2830; or letter to the Commissioner of Social Security, P.O. Box 17703, Baltimore, MD 21235–7703. You may also deliver them to the Office of Regulations, Social Security Administration, 107 Altmeyer Building, 6401 Security Boulevard, Baltimore, MD 21235–6401, between 8 a.m. and 4:30 p.m. on regular business days. Comments are posted on the Federal eRulemaking Portal, or you may inspect them on regular business days by making arrangements with the contact person shown in this preamble.

FOR FURTHER INFORMATION CONTACT: Marilyn Hull, Social Security Administration, 5107 Leesburg Pike, Falls Church, VA 22041–3260, 703–605–8500 for information about this notice. For information on eligibility or filing for benefits, call our national toll-free number, 1–800–772–1213 or TTY 1–800–325–0778, or visit our Internet site, Social Security Online, at *http://www.socialsecurity.gov*.

SUPPLEMENTARY INFORMATION:

Electronic Version

The electronic file of this document is available on the date of publication in the **Federal Register** at *http://www.gpoaccess.gov/fr/index.html*.

Explanation of Changes

We are dedicated to providing high-quality service to the American public. Today and for the foreseeable future, we face significant challenges in our ability to provide the level of service that disability benefit claimants deserve because of the significantly increased number and complexity of these benefit claims. Consequently, we are publishing a temporary modification to the procedures we follow in the administrative law judge (ALJ) hearings process in claims for Social Security disability benefits or SSI payments

[80] *O'Hagan,* 521 U.S. at 672–73.

[81] *O'Hagan* dealt with Rule 14e–3(a), which governed trading on non-public, material information in connection with a tender offer. *Steadman* dealt with Rule 206(4)–2, the investment advisor custody rule.

[82] *O'Hagan,* 521 U.S. at 673–74.

[83] *See Chevron U.S.A. Inc.* v. *Natural Resources Defense Council, Inc.*, 467 U.S. 837, 844 (1984). The Adopting Release states: ''Since the Commission is clearly authorized to prescribe [sic] conduct that goes beyond fraud as a means reasonably designed to prevent fraud, prohibiting deceptive conduct done negligently is a way to accomplish this objective.'' Adopting Release at Section II.D. This does not answer the question, however, of whether ''fraudulent, deceptive, or manipulative'' conduct can arise from negligent acts.

[84] Up until now under Section 206(4), we have done exactly this. We have adopted rules covering advertisements [17 CFR 275.206(4)–1], custody of client funds and securities [17 CFR 275.206(4)–2], cash payments for client solicitations [17 CFR 275.206(4)–3], disclosure of financial and disciplinary information [17 CFR 275.206(4)–4], proxy voting [17 CFR 275.206(4)–6], and compliance procedures [17 CFR 275.206(4)–7].

[85] *See* H.R. Rep. No. 2179 at 7 (1960) (identifying as the ''problem'' that Section 206(4) was intended to remedy: ''there has always been a question as to the scope of the fraudulent and deceptive activities which are prohibited and the extent to which the Commission is limited in this area by common law concepts of fraud and deceit.'').

[86] Adopting Release at Section II.D.

[87] Adopting Release at Section II.D.