



October 2, 2023

Vanessa A. Countryman  
Secretary  
U.S. Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549-1090

Re: Exemption for Certain Investment Advisers Operating Through the Internet (File Number S7-13-23); 88 Fed. Reg. 50076 (Aug. 1, 2023)

Dear Ms. Countryman:

Better Markets<sup>1</sup> appreciates the opportunity to comment on the above-captioned Proposed Rule (“Proposal” or “Release”)<sup>2</sup> to amend the exemption for certain investment advisers that provide advisory services through the internet (“internet investment advisers”) from the prohibition on Commission registration as an investment adviser.

The Proposal is an important reform to implement the framework Congress envisioned for dividing responsibility for regulating investment advisers between the Commission and the states. Congress envisioned a system whereby the Commission would regulate investment advisers with a national presence and the states would regulate investment advisers with a local presence. Under this approach, investment advisers must satisfy certain requirements to register with the Commission rather than the states. Although the Commission adopted a rule to allow internet investment advisers to register with the Commission rather than the states, that rule has allowed internet investment advisers to register with the Commission even when they do not have a national presence. The Proposal would help ensure that internet investment advisers have a national presence when they register with the Commission.

The Proposal would require that internet investment advisers have an operational interactive website to rely on the exemption allowing Commission registration as an investment adviser (“Internet Adviser Exemption”). Currently, the Internet Adviser Exemption does not require that an internet investment adviser’s interactive website be operational. As a result, some advisers registering with the Commission under the Internet Adviser Exemption have not actually provided investment advice to any clients through an interactive website for many years.<sup>3</sup> Such advisers with very few or no clients are more akin to local businesses that can be regulated by the

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<sup>1</sup> Better Markets is a non-profit, non-partisan, and independent organization founded in the wake of the 2008 financial crisis to promote the public interest in the financial markets, support the financial reform of Wall Street, and make our financial system work for all Americans again. Better Markets works with allies—including many in finance—to promote pro-market, pro-business, and pro-growth policies that help build a stronger, safer financial system that protects and promotes Americans’ jobs, savings, retirements, and more.

<sup>2</sup> 88 Fed. Reg. 50,076 (Aug. 1, 2023).

<sup>3</sup> Release at 50,080.

states.<sup>4</sup> The Proposal's requirement that internet investment advisers relying on the Internet Adviser Exemption have an operational interactive website would prevent advisers that do not actually provide investment advice through an interactive website from registering with the Commission.

The Proposal would also require that internet investment advisers provide investment advice exclusively through an interactive website to rely on the Internet Adviser Exemption. Currently, the Internet Adviser Exemption allows internet investment advisers relying on the exemption to provide investment advice through an interactive website and also through other means to fewer than 15 clients during the preceding 12 months. Because investment advisers are increasingly using technology to provide investment advice, more and more advisers are providing advice both through interactive technology and personal interactions.<sup>5</sup> But the Commission intended the Internet Adviser Exemption as a narrow exemption for entities that are in the business of only providing investment advice through an interactive website. The Proposal would limit the use of the Internet Adviser Exemption to those investment advisers whose business it is to provide investment advice to clients exclusively through an interactive website.

These amendments to the Internet Adviser Exemption would help to accomplish the original purpose of the exemption, which was to allow advisers that provide advice to clients exclusively through the internet, and therefore may have a national presence, to register with the Commission. The Commission should not devote its limited resources to regulating internet investment advisers that no longer provide investment advice through their interactive website or investment advisers who are really local in nature but who use technology along with human interactions to provide advice to clients. The amendments will allow the Commission to more appropriately allocate its resources to regulate investment advisers with a national presence.<sup>6</sup>

Still, the Commission should go further. The amendments would require that, to rely on the Internet Adviser Exemption, an internet investment adviser must provide digital investment advisory services through its operational interactive website to more than one client. That is not sufficient to ensure that the internet investment adviser has a truly national presence. Commission rules allow investment advisers to register with the Commission if they would otherwise have to register in at least 15 states. The Commission should require, under the amended Internet Adviser Exemption, that internet investment advisers provide digital investment advisory services through their operational interactive website to at least 15 clients to rely on the Internet Adviser Exemption to ensure that advisers registering with the Commission have a national presence.<sup>7</sup>

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<sup>4</sup> *Id.*

<sup>5</sup> *Id.* at 50,078.

<sup>6</sup> *Id.* at 50,080.

<sup>7</sup> Commission rules allow investment advisers expecting to be eligible for Commission registration within 120 days to register with the Commission. 17 C.F.R. 275.203A-2(c). The Commission believes internet investment advisers can use this "120-day" rule to develop, test, and launch an operational interactive website and obtain initial clients by the time the 120-day temporary registration expires. Release at 50,081. So the use of this provision would prevent internet investment advisers from having to register in multiple states while accumulating the minimum number of clients required by the Internet Adviser Exemption.

## **BACKGROUND**

The Commission originally adopted the Internet Adviser Exemption in 2002. It did so after Congress passed the National Securities Markets Improvement Act of 1996 (“NSMIA”). NSMIA amended the Investment Advisers Act of 1940 to divide the responsibility for regulating investment advisers between the Commission and state securities regulators. Congress allocated to state securities authorities the primary responsibility for regulating smaller advisory firms and to the Commission the primary responsibility for regulating larger advisers. Following further amendments to the Advisers Act in the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank”), investment advisers with less than \$100 million in assets under management are generally prohibited from registering with the Commission.<sup>8</sup> The requirement that investment advisers reach a certain threshold in assets under management to register with the Commission is meant to reserve Commission registration for investment advisers with a national presence, as opposed to advisers that are essentially local businesses that can be regulated by the states.<sup>9</sup>

Nonetheless, Congress provided the Commission with the authority to enable certain advisers to register with it despite managing less than \$100 million in assets. Section 203A of the Advisers Act provides that the Commission may permit investment advisers to register with it if prohibiting such registration would be unfair, a burden on interstate commerce, or otherwise inconsistent with the purposes of the Advisers Act. Under this authority, the Commission adopted the Internet Adviser Exemption as Advisers Act Rule 203A-2(f), which allows an internet investment adviser to register with the Commission if it provides investment advice to its clients exclusively through an interactive website, except that it may provide investment advice to fewer than 15 clients through other means during the preceding 12 months.<sup>10</sup>

The Commission’s intent in promulgating the Internet Adviser Exemption was to permit Commission registration for internet investment advisers who, unlike state-registered advisers, have no local presence and whose advisory activities are not limited to one or a few states.<sup>11</sup> Internet investment advisers provide investment advice to their clients through interactive websites, which clients visit to answer online questions concerning their personal finances and investment goals and which then provide advice after the adviser’s computer-based application or algorithm processes and analyzes each client’s responses. Clients residing in any state thus can, upon accessing the interactive website, obtain investment advice at any time.<sup>12</sup>

Because internet investment advisers do not manage the assets of their internet clients, they do not meet the minimum threshold for assets under management to register with the Commission.

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<sup>8</sup> Release at 50,077.

<sup>9</sup> *Exemption for Certain Investment Advisers Operating Through the Internet*, 67 Fed. Reg. 77620-01, 77620 (Dec. 12, 2002) (citing S. Rep. No. 293, 104th Cong., 2d Sess. 3-5 (1996) (Senate Report)).

<sup>10</sup> Release at 50,077-50,078. The Commission subsequently redesignated the Internet Adviser Exemption as Advisers Act Rule 203A-2(e). *Id.* at 50,077-50,078 n.14.

<sup>11</sup> *Exemption for Certain Investment Advisers Operating Through the Internet*, 67 Fed. Reg. at 77,620.

<sup>12</sup> *Id.*

Absent the Internet Adviser Exemption, they would have been required to register in all states (absent a state exemption) since anyone in any state could visit their website and receive investment advice at any time. The Commission adopted the Internet Adviser Exemption because it believed Commission registration for these internet investment advisers was more consistent with NSMIA's intent to allocate responsibility for advisers with a national presence to the Commission.<sup>13</sup>

Since the Commission adopted the Internet Adviser Exemption in 2002, investment advisers have increased their use of technology to provide investment advice. In addition to interactive websites, investment advisers now provide advice through mobile applications, investor portals, text messages, chatbots, and robo-advisers. At the same time as investment advisers' use of technology has increased, so has the number of investment advisers seeking to rely on the Internet Adviser Exemption. But the Commission intended the exemption to apply to advisers in the business of exclusively providing investment advice through an interactive website.<sup>14</sup> As a result, investment advisers are seeking to use the Internet Adviser Exemption to register with the Commission despite the fact that they may use technology but not have a national presence in the way that the Internet Adviser Exemption contemplates. That undermines the Commission's ability to use its scarce resources in a manner that best protects the public.

## **OVERVIEW OF THE PROPOSAL**

The Proposal amends the Internet Adviser Exemption in an attempt to ensure that only advisers with a national presence may register with the Commission. The Proposal requires that internet investment advisers relying on the Internet Adviser Exemption at all times have an "operational" interactive website. The Commission is also amending the rule to require that the Internet Adviser Exemption be available only to those advisers that provide advice exclusively to clients through an operational interactive website. Thus, the Proposal would eliminate the exception in the current rule that permits internet investment advisers to rely on the Internet Adviser Exemption while having up to 14 non-internet clients in a 12-month period.<sup>15</sup>

- With respect to the requirement that the internet investment adviser at all times have an operational interactive website, the Proposal defines an "operational interactive website" to mean a website or mobile application through which the investment adviser provides digital investment advisory services on an ongoing basis to more than one client. The Proposal defines a digital investment advisory service as a service that provides investment advice to clients where the advice is generated by the operational interactive website's software-based models, algorithms, or applications based on personal information each client supplies through the interactive website.<sup>16</sup> These definitions provide greater specificity than the current rule, which defines an interactive website to mean a website in

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<sup>13</sup> *Id.* at 76,621.

<sup>14</sup> Release at 50,078-50,079.

<sup>15</sup> *Id.* at 50,080.

<sup>16</sup> *Id.*

which computer software-based models or applications provide investment advice to clients based on personal information each client supplies through the website.

- With respect to the elimination of the exception in the current rule that permits internet investment advisers to have fewer than 15 non-internet clients in a 12-month period, the Commission now believes that an internet investment adviser advising any non-internet clients should not be exempted from the registration rules that otherwise apply to all investment advisers and should more properly be regulated by a state or states unless they satisfy a different basis for Commission registration. It is now easier for businesses that operate through the internet to track the locations in which they offer services. It is therefore easier for investment advisors that use the internet to interact with clients, but do not provide advice to clients exclusively through the internet, to keep track of the states in which they may be required to register if they do not qualify for Commission registration.<sup>17</sup>

## **COMMENTS**

### **I. The Commission should amend the Internet Adviser Exemption to better accomplish its goal of furthering Congress’s intent that only advisers with a national presence register with the Commission and other advisers register with the states.**

The Proposal represents an important reform to prevent investment advisers that use technology to provide investment advice but do not have a national presence from registering with the Commission. The requirement that an internet investment adviser must have an operational interactive website that provides digital investment advisory services on an ongoing basis to more than one client is intended to reflect that advisers with zero or one client are more akin to local businesses that can be effectively regulated by a state, consistent with Congress’s intent under NSMIA.<sup>18</sup> The elimination of the provision that allows internet investment advisers to register with the Commission while providing investment advice through means other than an interactive website to no more than 14 clients in the preceding 12 months also ensures that only investment advisers whose business it is to provide advice exclusively through an operational interactive website may register with the Commission under the exemption. This is consistent with the purpose of the exemption to allow Commission registration for internet investment advisers who have no local presence and whose advisory activities are not limited to one or a few states.<sup>19</sup>

The Proposal’s determination to require that an internet investment adviser have an “operational” interactive website is entirely appropriate. Otherwise, clients might be misled into

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<sup>17</sup> *Id.* at 50,083. It is also easier today for investment advisors that use the internet to interact with clients but do not do so exclusively to satisfy another requirement for Commission registration. Large advisers that increasingly use technology to provide advice to clients but do not do so exclusively are able to register with the Commission by satisfying the assets under management threshold.

<sup>18</sup> *Id.* at 50,081.

<sup>19</sup> *See generally id.* at 50,082-50,083.

entering into a relationship with an investment adviser that was able to tout itself as being a Commission-registered adviser but that did not actually have a website that could be used to provide investment advice. The proposed rule prevents investors from being led to believe that an adviser relying on the Internet Adviser Exemption has a national presence and conducts its business through the internet when this is not in fact the case.<sup>20</sup>

The Proposal's determination to prevent an adviser from relying on the Internet Adviser Exemption if its operational interactive website provides digital investment advisory services to only one client or to no clients is also entirely appropriate. The purpose of the Internet Adviser Exemption is to allow internet investment advisers that have a national presence but do not satisfy the threshold for assets undermanagement to nonetheless register with the Commission. Advisers that have zero or one client do not have a national presence. This reform also helps prevent advisers from misleading the public by conveying the impression that they advise clients via the internet when in fact they do not have a meaningful number of internet-based clients.<sup>21</sup>

The elimination of the exception that allows internet investment advisers to register with the Commission under the Internet Adviser Exemption but still advise up to 14 non-internet clients in a 12-month period is also crucial. Otherwise, an investment adviser could provide advice to two clients through an operational interactive website and 14 clients through other means, even if all of those clients were located in the same state, and still qualify for the Internet Adviser Exemption. This would frustrate the purpose of the exemption, which is to permit Commission registration for investment advisers that have a sufficient national presence while leaving it to the states to regulate investment advisers that have only a local presence. Investment advisers that communicate their investment advice to clients through interpersonal interactions should not be eligible for the Internet Adviser Exemption. Such advisers have a local presence with respect to their clients and accordingly should be regulated by the states, unless another basis for registration with the Commission would make those advisers eligible for such registration.

In this respect, the Commission should include in the final rule the Proposal's specification that to rely on the exemption the adviser must provide investment advice to clients that is generated by the website's software-based models, algorithms, or applications.<sup>22</sup> This means that the investment adviser's personnel cannot be responsible for the client-specific investment advice. Investment advisers should not be able to avail themselves of the exemption simply by virtue of delivering advice through electronic means where that advice was actually prepared by their personnel.

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<sup>20</sup> *Id.* at 50,088.

<sup>21</sup> *Id.*

<sup>22</sup> *Id.* at 50,081-50,082.

**II. The Commission should modify the Proposal to require that internet investment advisers provide digital investment advisory services through their operational interactive websites to at least 15 clients to rely on the Internet Adviser Exemption.**

Although the Proposal represents an important step in ensuring that Commission registration is reserved for advisers with a national presence, it does not go far enough. It eliminates the exception that allows internet investment advisers to rely on the Internet Adviser Exemption while providing investment advice to up to 14 non-internet clients, and it requires that internet investment advisers provide advice to clients exclusively through an operational interactive website. But it provides that the operational interactive website need only provide digital investment advisory services on an ongoing basis to more than one client. This means that internet investment advisers can rely on the exemption so long as they provide investment advice exclusively through their operational interactive website to only *two* clients. Such a modest numeric requirement will hardly serve as a reliable indicator that the adviser has a national presence. The Commission should, to ensure a national presence, require more than that an adviser provides advice through its operational interactive website to two clients.

Advisers Act Rule 203A-2(d) permits investment advisers to register with the Commission if they would otherwise have to register in at least 15 states.<sup>23</sup> As originally adopted, the rule permitted investment advisers to register with the Commission if they would have otherwise had to register in at least 30 states. Consistent with NSMIA's intended division of responsibility, the Commission believed that an investment adviser whose activities triggered registration requirements in at least 30 states was a national firm that the Commission should regulate.<sup>24</sup> The Commission subsequently amended the rule to allow Commission registration for an investment adviser that would otherwise have to register in at least 15 states, under the view that such registration requirements were sufficient to render the adviser a national firm that the Commission should regulate.<sup>25</sup> Although there is no guarantee that an internet investment adviser who provides investment advice through its operational interactive website to at least 15 clients would have its clients throughout the country, a requirement that the adviser provide advice through its website to at least 15 clients would come closer to ensuring that the adviser has a national presence and therefore should be regulated by the Commission, compared to the proposed requirement that the adviser provide advice through its website to just two or more clients.

The Proposal says that requiring an internet investment adviser to provide advice through its website to more than two clients to rely on the Internet Adviser Exemption would disadvantage advisers with a small clientele.<sup>26</sup> But investment advisers with a small clientele are not likely to

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<sup>23</sup> 17 C.F.R. 275.203A-2(d).

<sup>24</sup> *Exemption for Investment Advisers Operating in Multiple States*, 621 Fed. Reg. 61,866-01, 61,867 (Nov. 19, 1997).

<sup>25</sup> *Rules Implementing Amendments to the Investment Advisers Act of 1940*, 75 Fed. Reg. 77,052-01, 77,059 (Dec. 10, 2010).

<sup>26</sup> Release at 50,090.

have a national presence, so there is no reason to allow them to register with the Commission just because they provide their small clientele with advice through a website. The proposed approach would also be unfair to advisers who have a small client base but do not offer internet-based advice and therefore would be barred from Commission registration, absent some other exemption.<sup>27</sup>

### **III. The Commission must ensure that the responsibility for regulating investment advisers is divided between itself and the states in light of its scarce resources.**

The Proposal states that amending the Internet Adviser Exemption would further investor protection objectives by better allocating the Commission's resources to those advisers that should be subject to national rules.<sup>28</sup> This is especially important as those resources have become increasingly scarce in recent years. The scope and breadth of the Commission's responsibilities have increased dramatically over the last decade. And yet the agency's funding has failed to keep pace.<sup>29</sup> This means that the Commission must consider how best to use its limited resources.

The problem is particularly acute with respect to the regulation of investment advisers. The Commission has never had sufficient resources to regulate the large number of investment advisers in the United States.<sup>30</sup> Prior to NSMIA, the GAO identified the Commission's lack of resources as an important problem preventing the most effective oversight of investment advisers.<sup>31</sup> The amendments to the Advisers Act in both NSMIA and Dodd-Frank reflect Congress's decision that scarce Commission resources are best used to examine large investment advisers—those with a national presence—rather than the smaller investment advisers that may be regulated by the states.<sup>32</sup> The Proposal ensures that the Commission's resources are devoted to regulating investment advisers with a national presence, consistent with Congress's intent.

To be sure, the Proposal is not a substitute for providing the Commission with more resources to regulate investment advisers (and to further the other parts of its mission that are

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<sup>27</sup> The Proposal notes that investment advisers that use interactive technology to provide advice but would not qualify for the Internet Adviser Exemption would likely not have to register in every state, as was contemplated when the Commission first adopted the Internet Adviser Exemption. Since the exemption was originally adopted, it has become common for businesses to implement technology that targets and tracks the locations in which they offer services. As a result, today's investment advisers are better able to control in which states they may be required to register, if they do not qualify for Commission registration. Release at 50,087 n.89.

<sup>28</sup> Release at 50,080.

<sup>29</sup> Better Markets Month in Review Newsletter – April 2023 (Apr. 17, 2023, <https://bettermarkets.org/newsroom/better-markets-month-in-review-newsletter-april-2023/>).

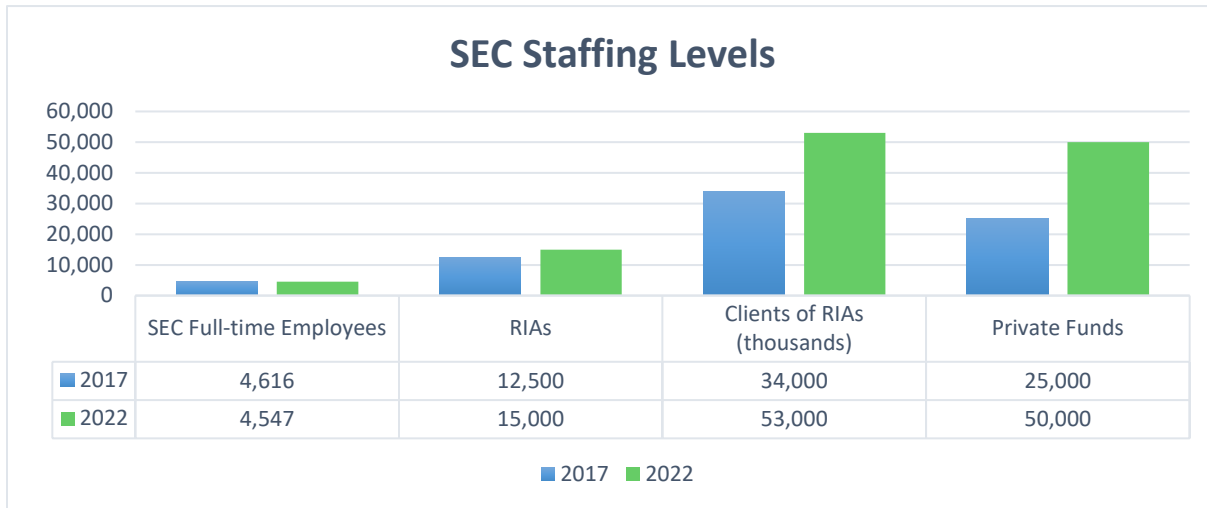
<sup>30</sup> Francis J. Facciolo, *Do I Have a Bridge for You: Fiduciary Duties and Investment Advice*, 17 U. PA. J. BUS. L. 101, 149 (2014).

<sup>31</sup> *Id.* at 150-51 (citing GEN. ACCOUNTING OFFICE (GAO), CURRENT LEVEL OF OVERSIGHT PUTS INVESTORS AT RISK 27, GAO/GGD-90-83 Investment Advisers (1990), <http://www.gao.gov/assets/150/149341.pdf>).

<sup>32</sup> *Id.* at 155.



critical to investor protection). As the below chart shows,<sup>33</sup> the Commission would still need more resources to regulate the rapidly expanding investment adviser industry. The SEC staff has actually shrunk in recent years while the number of registered investment advisers (“RIAs”), clients of RIAs, and private funds has grown substantially:



Nonetheless, the Proposal is necessary to allow the Commission to focus its efforts on regulating investment advisers with a national presence and ensure that the states regulate smaller advisers that have only a local presence regardless of their use of technology to provide advice.

## **CONCLUSION**

We hope these comments are helpful as the Commission finalizes the Proposal.

Sincerely,

Stephen W. Hall  
Legal Director and Securities Specialist

<sup>33</sup> See Better Markets, *SEC Staffing Levels Have Not Kept Pace with Growth of the Markets* (Apr. 14, 2023), <https://bettermarkets.org/analysis/sec-staffing-levels-have-not-kept-pace-with-growth-of-the-markets/>.

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