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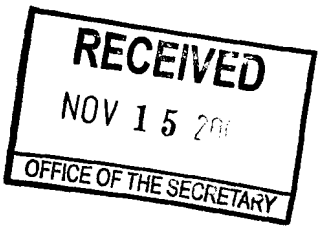


November 7, 2004

The Honorable William H. Donaldson, Chairman
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549-0609

Re: File No. S7-25-99; Proposed Rule: "Certain Broker-Dealers Deemed Not To Be Investment Advisers"

Dear Chairman Donaldson:

I am writing to respond to comments submitted to the Commission by the Securities Industry Association (SIA) regarding the proposed rule. This letter supplements the previous comments I have submitted on this important consumer protection issue.

1. Perceived Institutional Bias of SEC In Favoring Broker-Dealer Firms Over Consumers. Most troubling to me and many others in the evolution of this debate is the perception that SEC staff has favored the broker-dealer industry to the point of negating the primary purpose of the SEC - the protection of consumers. For example, in April 2004 I personally discussed the Proposed Rule with a key SEC staffer at a conference. The staffer, who mistakenly thought I was associated with a broker-dealer firm, informed me with a tone of cynicism that "the only ones that oppose the rule are those financial planners and a few consumer groups." The institutional bias of the SEC in favoring the broker-dealer industry, and ignoring the important protections of the Investment Advisors Act of 1940, can likewise be seen in the SEC's own consumer literature (available on its web site). Furthermore, when the SIA addresses its letter to the Chairman as "Dear Bill," such evidence of a close relationship does not serve to promote consumer confidence in the U.S. Securities and Exchange Commission.

2. The SEC By The Proposed Rule Thwarts The Will and Intent of Congress. By flawed logic the SEC staff has attempted to justify the Proposed Rule as fitting within the limited exception to the IA Act of 1940 which was provided by Congress.[1] Congress did not just specify that the performance of advisory

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[1] Section 202(a)(11) of the IA Act of 1940 clearly provides: "Investment adviser" means any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities; but does not include ... (C) any broker or dealer whose performance of such services is solely incidental to the conduct of his business as a broker or dealer and who receives no special compensation therefor;

services by broker-dealers had to be incidental, it went further and specified that the services had to be solely incidental. Then Congress went even further in specifying the additional requirement that the advisory services must not be provided for special compensation. As my earlier comments point out, no reasonable interpretation of this language can exist to justify the broad exemption proposed for fee-based accounts of broker-dealer firms. SEC staff should merely consult Webster's Dictionary should there be any doubt on the plain meaning and clear intent of the language contained in the IA Act of 1940.

3. The IA Act of 1940 Imposes An Important Protection for Consumers: A Broad Fiduciary Duty. The SIA goes to great length to seek to illuminate the volume of the rules and requirements imposed upon the actions of registered representatives of broker-dealer firms. It is not the quantity of the regulations that matters; rather, it is the quality of them. The broad fiduciary duties of due care and loyalty imposed by the IA Act of 1940 upon those who provide investment advisory services *dwarfs* all of the duties toward the consuming public which are currently imposed on broker-dealers. The SIA fails to recognize this important distinction. To paraphrase the recent comments submitted by the Consumer Federation of America, the SIA's position that fee-based brokerage accounts are already sufficiently regulated does not hold water. One need only look at the multitude of persistent and undisclosed conflicts of interests which continue to exist in the delivery of investment services to the consuming public to realize the lack of quality of broker-dealer regulation. Individual investors are entitled, by the IA Act of 1940, to receive investment advisory services which are in their best interests.

4. The SEC Should Not Be Seen As The Resistor To Marketplace Changes. Consumers increasingly seek out, and many demand, *truly* objective investment advice.[2] The marketplace should be allowed to function. The consumer marketplace desires investment advice which is provided in the best interests of the investor, not that which is in the best interests of the broker-dealer firm. The Proposed Rule is, unfortunately, an artificially created barrier against these forward-moving marketplace forces. By attempting to except broker-dealer fee-based accounts from the fiduciary duty standards of the IA Act of 1940, the SEC is seen as a tool of the broker-dealer industry, protecting it from changes demanded by the marketplace system. The marketplace forces of capitalism, and the continued disintermediation which has and will occur in the delivery of financial products to the consumer, should be permitted to work for the benefit of the individual investor. The SEC should not attempt to hold back the tide of these consumer-favorable developments through artificially-created barriers to change.

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[2] The major advertising campaigns of broker-dealer firms which tout the "objective advice" provided by stockbrokers might well be viewed as deceptive advertising, given the lack of full and detailed disclosure of conflicts of interest and fees, including those arising from payments by product manufacturers to brokerage firms.

5. The Uniformity of Securities Regulation Will Suffer Under the Proposed Rule. As stated in a letter submitted by the NASAA, "numerous states already require persons who 'hold themselves out' as providing investment advisory services to be registered as investment adviser." Moreover, many states define investment advisory services, and provide an exemption to broker-dealers, using nearly the same language set forth in Section 202 of the IA Act of 1940.[3] Should the Proposed Rule not be repealed and the Commission therefore not act to protect consumers, it seems readily apparent that state regulators will themselves act to safeguard the interests of the investment consumer. The states will likely apply their own existing state investment advisor laws to fee-based brokerage accounts. This will result in a further erosion of the important coordinated federal-state regulation of the securities industry, and also will open up the SEC to increased criticism as to its lead role as the champion of investor protection.

6. Important Questions Should Be Asked By The Commissioners At Upcoming Hearings On This Proposed Rule. Important questions should be asked of SEC staff and others who appear before the Commission on the upcoming hearings on this Proposed Rule. These questions include:

> What is the most reasonable interpretation of the statutory language contained in the IA Act of 1940? Will not the flawed interpretation of the Proposed Rule thwart the will of Congress?
>
> Why shouldn't fiduciary duties be imposed upon fee-based accounts of broker-dealer firms? What are broker-dealers afraid of? What is wrong with placing the best interests of the customer first? Why would a broker-dealer firm choose to not operate in a client-centric manner?
>
> Isn't it time for full disclosure of any and all conflicts of interest by those who seek to provide investment advice to the consumer, as required by the IA Act of 1940 (but not required by other regulations applying to fee-based broker-dealer accounts)? Moreover, should not firms seek to also minimize such conflicts of interest?

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[3] For example, the New York Investment Advisory Act provides the following definitions: "Investment adviser shall mean any person who, for compensation, engages in the business of advising members of the public, either directly or through publications or writings within or from the State of New York, as to the value of securities or as to the advisability of investing in, purchasing, or selling or holding securities, or who, for compensation and as a part of a regular business issues or promulgates analyses or reports concerning securities to members of the public within or from the State of New York. Investment supervisory service shall mean any person giving continuous advice as to the investment of funds on the basis of individual needs of each client." An exception is provided as follows: "a broker or dealer whose performance of these services is solely incidental to the conduct of its business as broker or dealer and who receives no special compensation for them ...."

If the Proposed Rule is repealed, will not brokerage firms proceed anyway with fee-based accounts, subject to the important consumer protections provided by the IA Act of 1940? Will not the investment consumer continue to seek out objective advice? Won't the competitive pressures on broker-dealers force them to change and provide accounts subject to the IA Act of 1940? Does not the Proposed Rule attempt to thwart this important and favorable change in the marketplace for investment advisory services?

How can the Proposed Rule, which effectively removes the most important protection provided to consumers of investment advisory services by the IA Act of 1940 (the imposition of the fiduciary duty standard), be justified given the primary mission of the SEC:

> "The primary mission of the U.S. Securities and Exchange Commission (SEC) is to protect investors and maintain the integrity of the securities markets. As more and more first-time investors turn to the markets to help secure their futures, pay for homes, and send children to college, these goals are more compelling than ever."

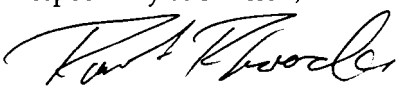
7. The Importance of This Issue Should Not Be Overlooked. As noted in my extensive comments (dated August 30, 2004) previously submitted to the SEC, the actions undertaken by the Commission with respect to this Proposed Rule will have a profound impact upon the investing public in the years ahead. All of the other important statutory, rule-making, and enforcement efforts of the past few years - analyst conflicts of interest, Sarbanes-Oxley reforms, mutual fund late trading reforms, etc. - are dwarfed by the impact of the resolution of this issue. ***All of the important functions of our system of regulation of the securities industry will, in the end, fail to adequately protect the consumer, should the SEC permit the final step in the delivery of the securities products to the consumer to be tainted by a failure to enforce the important fiduciary duties imposed by the IA Act of 1940 on those who seek to provide investment advisory services to the individual investor.*** Accordingly,

- I urge the Commissioners to address the issue of this Proposed Rule ***very seriously***.
- I urge the Commissioners to ***personally read*** the many comments submitted in connection with this proposed rule prior to hearings on this matter, including the illuminating comments submitted by major consumer organizations.
- I urge the Commissioners to ***ask tough questions*** of SEC staff and all those who appear before it in the upcoming hearings.

- I urge the Commissioners to adhere to its primary mission, to ***protect*** the investment public, and to ***not be subservient*** to the broker-dealer industry, regardless of how powerful the broker-dealer industry may be and regardless of how much influence they seek to assert over the SEC.

- Finally, I urge the Commissioners to ***adhere to the will of Congress***, the representatives of the people, not by twisting the ***plain language and clear meaning*** of the Investment Advisers Act of 1940, but rather by making it clear that the important ***fiduciary duty*** and other protections afforded to consumers by the IA Act of 1940 do, in fact, apply to fee-based brokerage accounts.

Respectfully submitted,



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