January 13, 2000

Jonathan G. Katz
Secretary
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549-0609

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

Dear Mr. Katz:

The Consumer Federation of America[1] appreciates this opportunity to comment on the Commission's proposed rule regarding broker-dealer's exclusion from the Investment Advisers Act. We agree that new developments in the brokerage industry -- including changes in broker-dealers' compensation methods -- make it appropriate to reexamine their exclusion from the Advisers Act. We also share the Commission's conviction that investors will benefit if broker-dealers can be encouraged to compensate their sales representatives in ways that minimize conflicts of interest. However, we do not support this proposed rule as a means of accomplishing that goal.

The Commission proposes to allow brokers who receive "special compensation" for investment advice to qualify for the broker-dealer exclusion, so long as the advice offered is "solely incidental" to the conduct of the broker-dealer's primary business, the advice is provided on a non-discretionary basis, and the broker-dealer discloses to clients that the account is a brokerage account. We believe this proposal conflicts with legislative language, reverses the Commission's own past interpretations of that language, and does so in a way that could have negative repercussions for investors beyond the issues raised in this particular rule proposal. The rule proposal is particularly troubling in light of the Commission's failure to enforce the exclusion's requirement that any advice be solely incidental to the broker-dealer's primary business, a failure that has left receipt of special compensation as virtually the only test for the broker-dealer exclusion. Finally, by pursuing a different approach, the Commission could accomplish its goal of allowing new compensation practices without these potentially negative

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[1] The Consumer Federation of America (CFA) is a non-profit association of more than 260 pro-consumer groups founded in 1968 to advance the consumer interest through advocacy and education.

consequences for investors.

I. Changing conditions in the financial services industry necessitate a new analysis of the broker-dealer exclusion.

The full service brokerage industry today finds itself at a crossroads. For two decades, full service firms have faced growing competition both from traditional investment advisers and from the financial planning industry, whose claim to offer comprehensive, objective financial advice has been an attractive selling point with the public. More recently, upstart on-line brokerage firms, with their rock bottom prices and high level of convenience, have begun to offer serious competition for self-directed investors. The result is that full service firms are being pulled in two very different directions. On the one hand, they must seek to satisfy those investors who want to complete their transactions quickly and conveniently at the lowest possible price. On the other hand, they must continue to attract those customers who want objective, professional financial advice.

Full service firms have adopted a number of strategies to compete for advice-seeking customers -- selling wrap accounts and offering computerized financial plans, for example. For more than a decade, however, their primary competitive strategy has consisted of aggressively marketing themselves to the public as if the principle service they offered were objective financial advice. While those campaigns would appear to have been at least partially successful, the firms' commission-based system of compensation conflicted with the image they were attempting to convey. Driven by a number of factors, then -- not least Chairman Levitt's leadership in raising issues of compensation-related conflicts of interest -- several full service firms have recently adopted fee-based services. In these programs, brokerage services are offered for a fixed fee or fee based on the amount of assets on account with the broker-dealer rather than being compensated through traditional commissions, mark-ups, and mark-downs. Meanwhile, to compete for self-directed investors, many of these same full service firms have begun to offer their own on-line execution-only services at reduced commission rates.

These new forms of compensation naturally raise questions about whether broker-dealers can be said to be earning "special compensation" for investment advice and whether they should therefore be subject to the Investment Advisers Act. It is these questions that the current rule proposal is designed to address. Specifically, the Commission has concluded that broker-dealers who adopt fee-based services and who charge lower commissions for on-line execution-only services are receiving special compensation for investment advice. In order to permit them to do so without triggering coverage under the Advisers Act, the proposed rule would eliminate receipt of special compensation for advice as an absolute test that precludes a broker-dealer from relying on the exclusion.

CFA does not share the Commission's interpretation that the compensation practices described in the rule proposal necessarily constitute special compensation for advice. Even if we did share that interpretation, we would not support this rule proposal as the best way to address that issue.

II. New compensation methods can be accommodated within the existing broker-dealer exclusion.

When Congress adopted the Investment Advisers Act in 1940, it offered an exclusion from the definition of investment adviser -- and thus from the regulatory requirements of the act -- to any broker or dealer "whose performance of [advisory] services is solely incidental to the conduct of his business as a broker or dealer and who receives no special compensation therefor."[2] In crafting this exclusion, Congress made it clear that they did not want all broker-dealers to be subject to the Advisers Act simply because they recommend the purchase and sale of securities. On the other hand, Congress made it equally clear that broker-dealers should not automatically be excluded from the act simply because they are already regulated as brokers. Specifically, Congress stipulated that broker-dealers should be subject to the Advisers Act under either of the following circumstances:

- they offer investment advice beyond that which is incidental to their regular business of effecting transactions in securities; or

- they receive special compensation for offering advice, even if the advice for which they are compensated is solely incidental to their regular business.

This language raises two questions, both of which are pertinent to the issues currently under consideration by the Commission. 1) What does it mean for a broker to offer investment advice that is "solely incidental" to its regular business? And 2) What constitutes special compensation for investment advice? In providing guidance on Congress's intent, the Senate Committee on Banking and Currency specified that the exclusion was available to brokers only "insofar as their advice is merely incidental to brokerage transactions for which they receive only brokerage commissions."[3] It is clear from this explanation both that Congress intended only a very narrow exclusion for broker-dealers and that Congress viewed the primary business of broker-dealers to be effecting transactions, not offering advice.

It appears to be this early Senate report language, rather than the legislative language itself, which has led to the focus on method of compensation in determining broker-dealers' right to rely on the exclusion. We do not believe, however, that this reference by the committee to "brokerage commissions" was intended to distinguish between commission-based compensation for brokerage transactions and fee-based compensation for the same transactions. Rather, it simply reflects the fact that, at the time the law was passed, broker-dealers were compensated for selling securities through commissions.

In an early decision on a related issue, the Commission reached the same conclusion. Shortly after the law passed, a question arose about "the status under the Investment Advisers Act of 1940 of over-the-counter brokers who charge an 'overriding commission' or 'service charge' on transactions involving the purchase or sale of listed securities through correspondent

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[2] Section 202(a)(11)©) of the Advisers Act.

[3] Committee on Banking and Currency, U.S. Senate, Investment Company Act of 1940 and Investment Advisers Act of 1940, Report No. 1775, 76th Congress, 3rd Session (June 6, 1940), pg. 22.

brokers who are members of a national securities exchange."[4] Because these over-the-counter brokers were being compensated through something other than standard "brokerage commissions," and because the compensation covered, at least in part, their advice with regard to those transactions, there was a question as to whether they were receiving "special compensation" for advice and thus should be subject to the Advisers Act. In deciding the matter, then SEC General Counsel Chester T. Lane made it clear that it was not the method of compensation that was the determining factor. Rather, he suggested:

> "The essential distinction to be borne in mind ... is the distinction between compensation for advice itself and compensation for services of another character to which advice is merely incidental."[5]

We believe this interpretation both accurately reflects the intent of Congress in crafting the broker-dealer exclusion and offers a model for determining how that exclusion relates to new compensation structures.

Following this reasoning, the first question the Commission should ask itself in deciding whether broker-dealers offering fee-based services should be excluded from the Advisers Act is whether the broker-dealer in question is offering investment advice through its fee-based program that fits within the solely incidental exclusion. In other words, is the advice being offered "merely incidental to brokerage transactions?"[6] If this is *not* the case -- if the broker-dealer is offering investment advice that goes beyond merely recommending the purchase and sale of securities -- then that broker-dealer is not offering "solely incidental" advice, as that phrase was meant by Congress, and is not entitled to rely on the exclusion, regardless of the

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[4] Opinion of General Counsel Relating to Section 202(a)(11)©) of the Investment Advisers Act of 1940, Investment Advisers Act Release No. 2 (Oct. 28, 1940), pg. 1. ("SEC Rel. No. IA-2.")

[5] Ibid., pg. 3. In elaborating on that interpretation, Lane concluded that a broker who "charges the overriding commission or service charge in every instance in which he transmits such an order to a member broker," and whose additional charges are "the same for all transactions of the same size, no matter who the customer is or how much consultation or advice the over-the-counter broker has given him," would be free to rely on the broker exclusion. His basis for drawing that conclusion was that, "[w]hile the time and expense involved in giving advice to customers may be among his motives for charging the overriding commission or service charge, they represent only one part of his general expenses, and are no more directly related to the charge which he makes than is similar advice given customers with respect to over-the-counter transactions for which the broker receives a regular commission."

[6] It is worth noting, in this context, that Congress specified that the advice had to be secondary to the transaction. It is not enough that the advice be generally related to the broker's primary business of effecting transactions. And, certainly, if the advice is the primary service being sold, it would not qualify as solely incidental.

method of compensation.[7]

If, on the other hand, the broker-dealer is offering only advice that is "merely incidental to brokerage transactions," the fact that a fee is charged rather than a commission should not automatically lead the Commission to conclude that "special compensation" has been received. Instead, the Commission should look at whether the fee is being charged for "advice itself" or for effecting transactions in securities, "to which advice is merely incidental."[8] As part of that determination, the Commission should follow Lane's example and examine: 1) whether the charges are "the same ... no matter who the customer is or how much consultation or advice" is provided and 2) whether there is any greater relation between the advice and the fee than there is between the advice and a standard brokerage commission.[9] If the fee charged is for effecting transactions in securities, and if it is applied uniformly to all customers in the fee-based program regardless of the level of advice offered the client, then the broker who offers a fee-based service should not be precluded from relying on the broker-dealer exclusion from the Advisers Act simply because of its method of compensation.[10]

The Commission should apply a similar deliberative process to brokers who charge lower commissions for on-line execution-only services. In this case, the question the Commission should ask is whether the key factor determining the difference in commission levels is the investment advice offered to the customer who deals with a registered representative. The Commission appears to have concluded that investment advice is the key differential. We do not agree that this is typically the case. The proof can be found in the fact that the customer who deals with a registered representative typically pays the same higher commission regardless of whether he initiates the trade or the broker makes a recommendation. Thus, it would appear that it is the privilege of dealing with a personal representative -- and the time that representative must spend servicing the account -- that justifies the higher commissions in most such cases.[11]

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[7] This is the same test that should apply to broker-dealers that charge commissions for their services. Being compensated by commissions should not automatically qualify the broker-dealer for the exclusion. The special compensation test is in addition to the solely incidental test, not a substitute for it.

[8] SEC Rel. No. IA-2, pg. 3.

[9] Ibid., pg. 2.

[10] Charging a lower percentage rate to customers with a higher level of assets on account would not constitute special compensation, since the difference in fee is not determined by the level of advice offered. If anything, the higher asset customer will require more advice, not less.

[11] If, on the other hand, a broker-dealer charged lower commissions for all execution-only services -- regardless of whether they are conducted on-line or through a registered representative -- then the Commission would be justified in concluding that the provision of advice was the key factor determining the different commission rates. In that case, the broker-dealer would clearly be receiving "special compensation" for advice and should therefore be subject to the Advisers Act.

III. The proposed rule is ill-advised and could be harmful to investors.

As we have described above, we do not believe the proposed rule is necessary to permit broker-dealers to adopt new compensation methods without losing their Advisers Act exclusion. Even if the Commission rejects our analysis on this point, however, it should not pursue this proposed rule. The rule conflicts with the legislation it is intended to implement; it does not offer adequate additional protections in limiting the "special compensation" test under the broker-dealer exclusion; and it would undermine important investor protections by freeing broker-dealers to charge their clients for investment advice without being regulated as advisers.

A. The proposed rule conflicts with the law it is intended to implement.

As we have noted above, Congress clearly intended to provide broker-dealers with only a very narrow exclusion from the Advisers Act, an exclusion that was not to be made available to any broker-dealer who receives special compensation for offering investment advice. From its earliest days, the Commission has supported this interpretation of the act's language regarding special compensation. In 1940, for example, the Commission issued a release stating that: "... that portion of clause (C) which refers to 'special compensation' amounts to ... [a] clear recognition that a broker or dealer who is specially compensated for the rendition of advice should be considered an investment adviser and not be excluded from the purview of the Act merely because he is also engaged in effecting market transactions in securities."[12] More recently, the Commission has concluded that if "a clearly definable part" of commissions received by the broker can be identified as compensation for investment advice, the broker is deemed to have received "special compensation" for advice and thus loses the right to claim the exclusion.[13]

In this proposed rule, the Commission has done an about face and now suggests that broker-dealers should, under certain circumstances, be allowed to receive special compensation for advice without being subject to regulation under the Advisers Act. However, the Commission cannot rewrite the law through the rule-making process, and should not attempt to do so. If, contrary to our analysis, the Commission determines that brokers who offer fee-based services or who charge lower commissions for on-line execution-only services are by definition receiving "special compensation" for advice, it has no choice but to implement the law as written and regulate those brokers as investment advisers or seek a legislative solution.[14]

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[12] SEC Rel. No. IA-2, pg. 3.

[13] Both SEC Rel. No. IA-1092 and *Investment Adviser, Financial Planners, and Others -- An Overview of the Investment Advisers Act of 1940*, by Robert E. Plaze, Division of Investment Management (undated), refer to the conclusion reached by SEC staff in Robert S. Strevel (pub. avail. Apr. 29, 1985) that "brokerage commissions generally would not constitute special compensation unless a clearly definable part of the commission is for investment advice (emphasis added). Rel. No. IA-1092, footnote 12. Plaze, pg. 6.

[14] CFA would strongly oppose legislation to eliminate the special compensation test for the broker-dealer exclusion from the Advisers Act. Our point here is simply that the special

B. The proposed rule does not offer adequate protections to substitute for the "special compensation" test.

For some time, the receipt of special compensation has been the primary characteristic determining whether a broker-dealer could rely on the exclusion from the Advisers Act.[15] The proposed rule now suggests that "the nature of the services provided," rather than the receipt of special compensation, should be "the primary feature distinguishing an advisory account from a brokerage account."[16] While we agree that the nature of services offered should be a determining factor, the proposed rule does not follow this idea to its logical conclusion and clearly specify what types of activities should qualify for the exclusion and what should not. Instead, the rule proposal suggests only one type of account that would not qualify for the exclusion, discretionary accounts that are charged an asset-based fee.

Problems abound with this approach. Not least is the inconsistency with which it applies the "special compensation" test for the exclusion. Brokers who charge an asset-based fee to operate a discretionary account would be subject to the Advisers Act, because those accounts "bear a strong resemblance to traditional advisory accounts," while brokers who offer the identical services for commissions would be excluded from the act because they receive no "special compensation" for advice.[17] [18] But, if the nature of services offered, rather than the compensation method, is to be the primary feature distinguishing an advisory account from a brokerage account, then these two accounts should clearly be treated the same.[19] As written, the rule proposal creates the strong impression that, while receipt of special compensation does not always preclude a broker-dealer from relying on the exclusion, failure to receive special compensation automatically permits the broker-dealer to rely on the exclusion. This is clearly the exact opposite of what Congress intended.

The real problem, as the above example helps to demonstrate, is that the Commission has failed to clarify what does and does not constitute solely incidental advice. Worse, the

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compensation test is embedded in the law itself and, thus, it cannot be changed through the rule-making process. Legislation is necessary to change the law.

[15] Plaze, pg. 6.

[16] Proposed Rule S7-25-99, pg. 5.

[17] Ibid.

[18] This would have the perverse effect of affording investors stronger protections when brokers use compensation systems that more closely align their interests with their customers' than those same investors would receive when the compensation system creates substantial conflicts of interest.

[19] Specifically, they should both be treated as advisory accounts, because they involve an extraordinary degree of reliance by the investor on the broker-dealer's advice. Advice in such circumstances is not, or should not be, merely incidental to sales transactions.

Commission has over at least the last decade allowed broker-dealers virtually free rein to abuse this provision of the exclusion. An early example can be found in an old Shearson-Lehman ad, which told the reader to "Think of your Shearson-Lehman Financial Consultant more as an advisor than a stockbroker."[20] But one need not look so far back to find examples of how brokers market themselves to the public as if the primary service they had to sell were advice.

- A current Merrill Lynch ad quotes a Leading Discount Broker's Investment Tip # 3, "For some investors, particularly those with a large or complex portfolios who want on-going investment management, the services of a fee-compensated financial advisor may be appropriate," then concludes, "Amen."[21]

- A Morgan Stanley Dean Witter ad is headed with a quote from Proverbs, "A wise man listens to advice." The ad then continues: "Usually, when you buy a mutual fund, all you get is a mutual fund. But when you buy a Morgan Stanley Dean Witter mutual fund, you get something extra: sound financial advice. Because our funds are only available through our Financial Advisors. Before making any recommendations, they'll first help you identify your financial goals, then give you tailored advice to help you meet them."[22]

- A Prudential Securities ad proclaims that "it's advice, not execution, that's at the heart of our relationships ..."[23]

It is difficult to conclude from these ads that any advice being offered is "merely incidental to brokerage transactions." In short, either these broker-dealers are offering advice that far exceeds the "solely incidental" advice that Congress envisioned as qualifying for the broker-dealer exclusion, or they are misrepresenting their services to investors.

Traditionally, broker-dealers have argued that -- their advertisements to the contrary -- they do not in fact offer anything more than solely incidental advice. Therefore, they argue, they should be regulated according to what they actually do, not according to how they market their services. We disagree. The Commission has interpreted that such "holding out" to the public would preclude an accountant or attorney from relying on their solely incidental exclusion, since it creates the appearance that the investment advice is more than solely incidental.[24]

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[20] See attached ad taken from the June 5, 1991 issue of *The New York Times.*

[21] See attached ad taken from the December 15, 1999 issue of *The Wall Street Journal*.

[22] See attached ad taken from the October 1999 issue of *Smart Money*.

[23] See attached ad taken from the February 2000 issue of *Kiplinger's Personal Finance.*

[24] SEC Rel. No. IA-1092 states on page 12, "The staff's view is that the exclusion contained in Section 202(a)(11)(B) is not available, for example, to a lawyer or accountant who holds himself out to the public as providing financial planning, pension consulting, or other financial advisory services. In such a case it would appear that the performance of investment

Unfortunately, the Commission has not taken a similar position on holding out by brokers, where, as the above examples demonstrate, the potential for confusion is enormous and the need for action is pressing. Instead, the Commission has maintained that broker-dealers can hold themselves out to the public as financial planners or advisers, as long as they only offer advice in their capacity as registered representatives and don't receive special compensation for advice.[25] Under the proposed rule, broker-dealers would get a new benefit. They could hold themselves out to the public as advisers, they could offer advice or claim to offer advice that clearly exceeds that which Congress intended to exclude from the Adviser's Act, they could charge their customers a fee that they identify as being a fee for advice, and they would still be regulated as salespeople. This is so clearly inappropriate it is difficult to see how the Commission could even propose it.

The Commission does raise this issue in the rule proposal when it notes that: "Some broker-dealers offering these new accounts have heavily marketed them based on the advisory services provided rather than the execution services, which raises troubling questions as to whether the advisory services are not (or will be perceived by investors not to be) incidental to the brokerage services."[26] Certainly this is the case in the Merrill Lynch ad mentioned above and even more so in the Prudential Securities ad for its Prudential Advisor program, which states, "Get personal advice without the traditional sales commission. With Prudential Advisor... you pay a simple asset-based fee for the advice you get and a low price for trades."[27] When the primary service being sold in a broker-dealer's ad is advice, and when the ad specifies that the fee you pay is for advice, of course investors will expect that advice is more than just an incidental sideline to the broker-dealer's primary sales business.

Therefore, if the Commission proceeds with this rule proposal, it should, at a minimum, preclude advisers from relying on the rule if they market the accounts in ways that suggest they are advisory accounts. However, the problem is broader than the rule proposal suggests, and the solution should be as well. What is really needed is for the Commission to apply the same standards to brokers that it applies to accountants who wish to rely on their solely incidental exclusion from the Advisers Act: it should clarify that brokers who hold themselves out to the

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advisory services by the person would not be incidental to his practice as a lawyer or accountant." In *Investment Advisers, Accountants, and Others*, Plaze elaborates on the same question, as follows, "The key determination under this exception is whether advice is provided solely incidental to the profession, and the staff looks to the following factors: does this person hold himself out to the public as an advisor or financial planner or as providing pension consulting or other financial advisory [services] -- if so, the exception is not available." (Plaze, pg. 6)

[25] Plaze, pg. 7. "The SEC staff has stated that a registered representative who holds himself out to the public as a financial planner cannot rely on the broker-dealer exception *unless he receives no special compensation therefor and gives investment advice solely in his capacity as a registered representative."* (Emphasis added.)

[26] Proposed Rule S7-27-99, pg. 5.

[27] See attached ad.

public as advisers or as providing advisory services will be regulated under the Advisers Act.[28]

Although the rule proposal includes a disclosure requirement designed to ensure that investors understand the nature of the account being offered and not confuse it with an advisory account, that requirement cannot adequately substitute for enforcement of the solely incidental portion of the exclusion. Based on our understanding of the knowledge and sophistication of the average investor, we are convinced most investors will not understand the significance of the disclosure. Specifically, we do not believe the average investor understands that a brokerage account is not an advisory account and that a broker is not an adviser. Certainly, they cannot be expected to understand this fact if the ad the disclosure is required to accompany either strongly implies or specifically states that the broker is an adviser and that the primary service being offered is advice.

If disclosure is to have a hope of being effective, then, it must clearly spell out the fact that any advice being offered is solely incidental to sales transactions and that it is not subject to a requirement that the salesperson place the client's interests ahead of his or her own. Even if the disclosure requirement were strengthened, however, we do not believe that disclosure alone offers adequate protections against misrepresentation and the investor confusion that inevitably results. Such a disclosure, no matter how prominent, cannot begin to outweigh the expectations raised by multi-million-dollar ad campaigns of the type described above.

C. The proposed rule would undermine investor protections by freeing brokers to offer investment advice for compensation without being regulated as advisers.

While the Investment Advisers Act of 1940 is a minimalist law, it does afford investors some important protections. At the heart of the act is "the notion that an adviser owes its clients a fiduciary obligation which is intended to eliminate conflicts of interest and to prevent the adviser from overreaching or taking unfair advantage of a client's trust."[29] As a fiduciary, the investment adviser "is held to something stricter than the morals of the market place. Not honesty alone but the punctilio of an honor the most sensitive, is then the standard of behavior."[30] This is clearly a far higher standard of conduct than that contained in the "suitability rule" that governs broker-dealers' sales recommendations. Similarly, the Advisers Act imposes an obligation to disclose material information -- such as the existence of conflicts of interest that may bias the adviser's recommendations, prior disciplinary problems that may reflect on the adviser's integrity, as well as extensive information regarding how the adviser conducts his or her business -- to which broker-dealers are not subject.

CFA believes that the broker exclusion crafted by Congress is a good one. Like the

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[28] The Commission should also examine these claims about the advisory services being offered to determine whether they are misleading.

[29] Plaze, p. 14.

[30] Justice Cardozo's opinion in Meinhard V. Salmon, 249 N.Y. 458, as cited in Plaze, p. 15.

members of Congress who overwhelmingly approved it, we believe broker-dealers who are compensated as advisers should also be regulated as advisers, as should broker-dealers who offer advice that goes beyond simply recommending the purchase and sale of securities. The proposed rule offers no justification for holding broker-dealers to a lower standard of conduct when they offer advice that exceeds these limitations than the standard their competitors in the investment advisory and financial planning industries must meet. We believe such a distinction is unjustified and will result in harm to investors, particularly if broker-dealers remain free to compete by portraying themselves as advisers while being regulated as salespeople.

IV. Conclusion

Market forces are increasingly forcing broker-dealers to compete as investment advisers. This has the potential to benefit investors who want recommendations that are more than merely suitable and who want advice that is more than merely incidental to a sales transaction. Investors will only benefit, however, if the increasingly advice-driven services offered by full service brokers are held to an advisory standard -- particularly a fiduciary duty to place clients' interest ahead of their own and an accompanying responsibility to fully disclose any and all potential conflicts of interest. The proposed rule would impede this development by allowing broker-dealers greater latitude to compete as advisers without subjecting them to regulation as such. We strongly oppose its adoption.

Instead, we urge the Commission to identify those broker-dealers that offer investment advice that exceeds the solely incidental standard, or who hold themselves out as offering such advice, and subject them to regulation under the Advisers Act. As part of that effort, the Commission should clearly and comprehensively spell out what does and does not constitute solely incidental advice under the broker-dealer exclusion from the Advisers Act. In doing so, the Commission should remain true to the very narrow definition of solely incidental advice intended by Congress. If the Commission were to pursue this approach, we believe that most of those full service brokers offering fee-based services would be swept under the act, not because of any changes in their compensation method, but because the advice they offer and the way they promote that advice do not qualify for the solely incidental exclusion.

Finally, to clarify how the exclusion applies to new compensation methods, the Commission should simply specify that it is not the method of compensation that determines the right to rely on the exclusion but whether a specific portion of that compensation is clearly identifiable as special compensation for investment advice. We believe this could be accomplished through a policy statement without need for a new rule proposal. In fact, such a policy statement from the Commission, one that clearly lays out all the issues related to the broker-dealer exclusion, would offer substantial benefits for investors, by eliminating widespread abuses of the exclusion, and for industry members, by eliminating any confusion about what services qualify. Broker-dealers who offer only solely incidental advice would then be free to offer fee-based services without triggering regulation as advisers so long as those fees were not misidentified as fees for advice.

We appreciate your attention to our concerns. If a member of the Commission or the Commission staff would like to discuss these issues further, we would be happy to do so. You

can contact me at 719-543-9468.

Sincerely,

Barbara L. N. Roper
Director of Investor Protection