

STATEMENT OF JOSEPH R. RUSSO, SEC RULE 12B-1 ROUNDTABLE  
Tuesday, June 19, 2007

I am Joe Russo, a native of Cedar Rapids, Iowa. I began my securities career in 1972 as a registered representative and have spent the past 35 years serving the investment needs of middle income clients. Today I do so as Advantage Financial Group, the premier Office of Supervisory Jurisdiction affiliated with the independent broker-dealer National Planning Corporation. We manage over \$1.5 billion of client assets within our 28 branch offices.

In the U.S., there are approximately 105,000 independent financial advisors like myself located in communities across the country serving more than 15 million American households. Approximately 20 percent of all registered representatives service their clientele through an independent broker-dealer. These financial advisors are independent contractors, rather than employees of the Independent Broker-Dealer firms. We provide comprehensive and affordable financial services that help millions of individuals, families, and small businesses with financial education, planning, implementation, and investment monitoring. Clients of independent financial advisors are typically "Main Street America." Independent financial advisors get to know their clients personally and provide them financial advice in face-to-face meetings – oftentimes over the client's kitchen table. Mutual funds purchased by check and application are often the appropriate investment choice for these clients. Due to their close ties to the communities in which they operate their small businesses, these financial advisors have a strong incentive to make the achievement of their clients' investment objectives their primary goal.

Many of the participants in today's roundtable are perhaps more qualified to discuss the historical basis for 12b-1 fees, fund director's oversight obligations under the Rule, and similar topics. However, as an independent financial advisor, I am uniquely qualified to speak about the client impact of Rule 12b-1 because of my direct knowledge of the important role it plays in my ability to service middle class Americans. I believe that the consequences of eliminating or drastically altering Rule 12b-1 would be disastrous to investors and, therefore, should trump all academic discussions of the relative merit of the Rule.

The simple fact is that middle class Americans need the continuing service, guidance and support that are provided by these independent financial advisors to achieve their stated investment goals. 12b-1 fees provide a tax efficient means to support the continuing service which these clients require for successful investing. The benefits of 12b-1 fees are numerous and include:

- Expanding Investor Choice - The multiple share classes made possible by Rule 12b-1 give investors choices by providing them with options in how they pay their financial advisor. The flexibility provided by Rule 12b-1 allows financial advisors to tailor a portfolio to their client's specific needs.
- Supporting Financial Literacy - Mutual funds send their investors monthly statements, confirmations, prospectuses, annual reports, and other materials. Financial advisors serve the vital role of educators by helping investors to make sense of these essential materials. 12b-1 fees are the compensation financial advisors receive for these efforts.
- Managing Client Expectations – We all know the common mistakes investors make; buying high and selling low, chasing past performance and harboring unrealistic

expectations. 12b-1 fees provide financial advisors with compensation to manage their client's expectations and protect them from making rash decisions.

- Insuring Small Accounts Receive Service – Investment advisory services are simply out of the reach of many small account holders. Financial advisors must have another means of being fairly compensated for serving these accounts. 12b-1 fees provide the mechanism to insure small investors receive the support and service they need to achieve their financial goals.
- Subsidizing Additional Services – Independent financial advisors offer their mutual fund clients a variety of additional services including: consolidated account statements, periodic portfolio review meetings, quarterly newsletters, cost basis research, preparation of tax returns, and consulting on other financial decisions. These important services are made possible by the subsidy 12b-1 fees provide.

Elimination or the drastic curtailment 12b-1 fees would have devastating unintended consequences for investors. Limiting investor choice, removal of the incentives to promote financial literacy and manage investor expectations, and the loss of the additional services I described are just the tip of the iceberg. In fact, significant changes to Rule 12b-1, combined with other recent events, including the uncertainty of fee-based brokerage accounts, may change the very nature of the financial services industry. Financial advisors are already approached with frequent pitches to drop their broker-dealer affiliation and eliminate the burdensome, confusing and ever changing securities regulatory environment by becoming investment advisors. While some may see this as a positive step, they fail to consider certain important real world implications – most notably, the damage this seismic shift would have on the current regulatory system. Just consider the following consequences of moving large numbers of registered representatives to the investment advisor supervisory structure:

- Registered representatives are subject to close supervision by their broker-dealer which has a financial incentive to insure they are compliant. Once they become investment advisors, these individuals would become responsible for supervising their own activities, or for hiring and firing their own compliance staff.
- Registered representatives' securities product sales are reviewed by their broker-dealer's trained compliance personnel to insure they are suitable for the client. The recommendations made by most retail investment advisors are reviewed by a CCO who is frequently employed by the advisor.
- In most cases, registered representatives are subject to annual on-site audits of their activities by their broker-dealer. Securities regulators audit a small retail investment advisor's office periodically -- perhaps once every 3-5 years.

These are just a few examples of the potential harm, and I could go on, but the reality is that the regulatory community is ill prepared for the transformation of the securities industry that is the likely unintended consequence of the elimination of 12b-1 fees.

The Commission is to be commended for initiating a comprehensive review of Rule 12b-1. This is an area of utmost importance to millions of investors – including those in my hometown. Rule 12b-1 was designed to enhance the value of fund ownership by attracting more investors into mutual funds. Independent financial advisors have reacted by providing additional services and support to their mutual fund clients. It is clear that Rule's purpose has been served by

facilitating these services. Any potential changes should be considered with an eye to reinforcing these important achievements.