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

6

February 20, 2003

Regarding: File No.: S7-03-03

Dear Mr. Katz:

I am an employee who manages compliance at a mid-sized investment advisor/investment company. I believe that adoption of the proposed rule requiring investment advisors and investment companies to adopt and implement compliance policies and procedures reasonably designed to prevent violations of federal securities laws, to be overseen by a designated chief compliance officer and subject to annual review, would be a significant and positive step toward protecting investors' assets for the following reasons:

- Investor's assets are not as secure as some quarters of the industry would have you believe. The element of misappropriation of assets, at even the largest organizations, is always present. A more common threat to the value of assets is the pricing of certain securities. Fair valuation of certain equities of illiquid companies, foreign securities, fixed income instruments, and alternative investments such as venture capital, private equity and real estate, is difficult to calculate and fraught with conflicts of interest. There is a strong incentive for some in the industry to willfully inflate the prices of such assets or ignore published guidance from regulators and accountants on how to fair value such assets. The proposed rule will greatly protect investors from a sudden drop in the value of their assets because the unmistakable legal obligation to accurately value such securities according to objective securities laws and other available guidance. The lesson of the Heartland Funds debacle should erase any doubt of the importance of accurate and objective valuation of assets.

- The rule would foster a more level playing field for investment advisors and investment companies. Some elements of top management at my firm would like to be more responsive to my efforts to foster compliance on particular issues, but sometimes they respond 'everyone else is doing it' or 'it's a business decision.' The proposed rule enhances accountability for compliance with federal securities laws equally for all firms and increases the attractiveness of compliance as a better choice for those who are reluctant see it as such.

- Many investment advisor and investment company compliance personnel, especially those employed by smaller firms, are engaged in other business activities unrelated to compliance. Therefore, they frequently do not have adequate time and resources to devote to the function. Still worse, some portfolio

managers and top managers at many firms do not take the compliance function seriously. The rule would be beneficial because it would focus attention on the importance of complying with federal securities laws and elevate the role of compliance at investment advisors and mutual funds. Unfortunately, many firms will not devote resources to this important component of the business unless they are required to do so.

- At many firms, there is a lack of knowledge about the requirements of the securities laws and how they affect the particular firm. Because the proposed rule focuses attention on the importance of compliance, firms will devote more resources to compliance.

I also support an expanded role by independent third parties in fostering compliance by investment advisors and investment companies with the federal securities laws for the following reasons:

- As noted above, many smaller advisors and funds have not devoted adequate resources to the compliance function or have not reached a size that would warrant hiring a dedicated compliance officer. Therefore, support from third-party compliance experts can assist many companies to identify particular rules that apply to the company and design a compliance program. Outside legal counsel is useful in drafting policies in response to rules and to answer legal questions, but it is up to in-house compliance staff to interpret how the rules affect each particular business. Outside compliance experts can assist in this task but many advisors and funds will forego contracting an outside expert unless they are required to do so.

  For example, I once suggested to top management that our firm undergo a compliance review by a consultant. I believed that a third-party's comments on compliance lapses would be beneficial because they would substantiate the importance of compliance. The request, however, was declined.

  It is important that the third party conducting the compliance review is truly independent. We have seen numerous instances in 2002 of the conflicts of interest that independent accountants and their affiliated consultants face. I have doubts, therefore, that the independent public accountant who currently conducts the annual audit of the fund, or a consultant affiliated with the auditor, would be sufficiently independent to conduct the compliance review. The current auditor/affiliated consultant may be reluctant to raise difficult compliance questions for fear of endangering the overall relationship it has with the company.

- The second possibility for comment noted in the proposal, the inclusion of an examination of compliance controls by the independent public accounts in connection with the current audit, has touched on what I have felt to be a significant weakness of the current annual audit regimen. Although the auditors are reviewing a full year in connection with the income statement, the efforts for

the balance sheet are focused on one day only. In anticipation of the audit for that day, I have seen securities moved off in-house pricing models to third-party pricing sources prior to the auditors' arrival, and moved back to the in-house pricing models subsequent to their departure.

Although the affect of the audit is that securities will probably be accurately priced by independent, third-party sources around the date tested by auditors, the current review does not prevent abuses the rest of the year. That is because the auditors do not conduct a broad test for controls of how securities are priced and other factors affecting the NAV. They merely test for the accuracy of the securities' prices and calculation of NAV for one day of the year.

Inclusion of an audit of controls to price securities and otherwise derive the NAV and balance sheet is critical to ensuring an accurate NAV and balance sheet throughout the year. Under Sarbanes-Oxley, the SEC currently requires the CEO and CFO to certify the accuracy of filings twice a year. This may be insufficient due to a technical view, at my company anyway, that the certification is limited to the two dates each year for which a balance sheet is submitted. Therefore, there is reduced vigilance to ensuring the accuracy of the NAV/balance sheet for the remaining days of the year.

In summary, I believe that the independent public accountants should include in their annual audit a review of controls to derive the NAV and the balance sheet. I am doubtful, however, that the independent auditor or an affiliated consultant is in the best position to conduct a regulatory audit of compliance controls firm-wide. I believe that the compliance controls audit should be conducted by a different independent public accountant or an independent consultant that specializes in such reviews.

- The formation of one or more self-regulatory organizations to oversee the activities of advisors and funds is a development that is long overdue. All other companies in the investment field including futures trading firms, broker-dealers, municipal bond traders, and the securities exchanges, are regulated by SROs. The inspection arrangement seems efficient because the SROs can focus on routine examinations while the agencies exercising oversight can focus on serious issues that are raised by the SRO examinations. Only advisors and funds are not subject to reviews by an SRO. Although I believe that the SEC's examination staff is dedicated, they simply are stretched too thin to adequately oversee the industry. Also, my experience is that they do not appear to have the time to delve into very complex or gray conflict of interest issues.

- Lastly, I believe that requiring advisors to obtain fidelity bond coverage would protect investors' assets. Funds are required to do so, as well as advisors that manage ERISA assets. The clients of all advisors deserve the same protections as fund shareholders and pension plan participants.

As a final note, many in the industry will complain that the additional protections will be too costly to implement. Rest assured that the industry can well afford to implement additional protections of clients' assets and the benefit of increased protection of investors' assets far exceeds the incremental financial cost. The ultimate affect, as they say, will be to keep honest people honest.

Sincerely,

A compliance officer who believes that integrity in the investment advisor and investment company industry is critical to serving the best interests of clients and shareholders.