

March 31, 2004

Jonathan G. Katz
Secretary
Security and Exchange Commission
450 Fifth Street
Washington DC 20549-0609

RE: File No. S7-04-04

Dear Secretary Katz:

This letter follows our March 10 comment letter re: S7-04-04. In our March 10 letter we recommended the SEC adopt the tenets of the Uniform Prudent Investor Act as the basis for a Code of Ethics. Today we urge the Commission to receive additional comment on questions that arise from the submitted comments. Specifically, we suggest that additional comment address a central issue: The Commission seeks a code reflecting “the advisor’s fiduciary obligations” – yet it does not define this “obligation.” How can advisers be expected to fulfill this obligation, if the Commission does not explain what it is, and what fiduciaries do?

Background

As you know, Chairman Donaldson has spoken often, eloquently and forcefully about the critical significance of advisers’ fiduciary duties. As the Chairman stated on January 14, “It is extremely troubling that so many of the recent scandals in the mutual fund industry have involved a breach of the fiduciary relationship between investment advisers and their advised funds. As fiduciaries, advisers owe their clients more than mere honesty and good faith. What we are seeing leads me to believe that all too many advisers have been delivering much less.”

The Commission’s introduction narrative seeking comment on the proposed Code reflects these sentiments completely, stating, “Advisers are fiduciaries that owe their clients a duty of undivided loyalty.” It closes by noting its proposed rule is “Designed to prevent fraud by reinforcing fiduciary principles that must govern the conduct of advisory firms and their personnel.” Further, the Commission notes in discussing its proposed standards of conduct, “This standard must reflect the advisor’s fiduciary obligations....”

The Commission asks, “Is our formulation of the business conduct element of the code of ethics appropriate? Should we specify a particular standard of conduct that all codes of ethics must incorporate? What standard should we adopt? Should the code of ethics require supervised persons comply with all applicable laws and regulations, ..(or) only federal securities laws?”

We reviewed the comments of the major professional associations for a central issue: how do they recommend that an SEC Code encourage, provide incentive, or require advisers’ fidelity to fiduciary standards. These groups are: North American Securities Administrators Association, the Financial Planning Association, the CFP Board of Standards, the National Society of Compliance Professionals, and the Investment Counsel Association of America.

Association Comments

The North American Securities Administrators Association (NASSA) does not express support for investment advisors being held to fiduciary standards; instead it expresses support for only for the “Commissions *desire* (emphasis added) to .. hold (advisers) accountable for their violations of their fiduciary obligations.” However, it opposes “a regulatory mandate of a written Code of Ethics” because such a code is not “the most appropriate method for ensuring compliance with the existing fiduciary duties of investment advisors.” Instead NASSA recommends the Commission “consider similar rules” to its own “model rules” adopted in 1997.

The Financial Planning Association (FPA) does not express support for fiduciary Standards. Instead FPA expresses support for its own “FPA Code of Ethics” and explains how the proposed SEC code is not necessary because it “duplicates” its Code. “We do not believe that CFP certificants should be required to adopt redundant provisions in the code of ethics they would be required to adopt under the proposed rule. We propose instead that CFP certificants be permitted to incorporate by reference the CFP Board Code of Ethics and *include in the SEC-required codes only those provisions that do not have an analogue in the CFP Board Code of Ethics.*” (Emphasis added)

The Investment Counsel Association of America expresses conceptual support for fiduciary responsibilities, noting that it has “endorsed standards emphasizing an investment adviser’s fiduciary duty”. Also, it is currently developing a model code of ethics that, among other purposes, seeks to “help educate advisory personnel of their fiduciary responsibilities.” However, the association opposes the SEC suggesting “particular standards of conduct” and urges it to instead adopt a “flexible approach” that allows individual members of the profession to “tailor their codes of ethics to accommodate their... business activity.”

The National Society of Compliance Professionals (NSCP) expresses strong conceptual support for fiduciary principles. However it opposes “a specific standard of conduct for all codes” or “any specific procedures in the proposed rule.” NSCP explains, with “the great diversity among investment advisers, NSCP does not believe that a single rule can be crafted that adequately addresses the potential conflicts of interests faced by this diverse group.”

The CFP Board of Standards “strongly supports the Commission’s proposal calling for an investment advisor code of ethics.” In its discussion of “Code of Ethics and Professional Responsibility” and “Standards of Conduct and Compliance with Laws” there is a detailed discussion of the history and effectiveness of the CFP Board’s Code of Ethics and “Practice Standards.” It is noted that when CFPs agree to abide by its Code, “Certificants have agreed to provide personal financial planning in the clients best interest and to act in accordance with the highest ethical and professional standards for the practice of financial planning.” However, no where in these discussions is there even a mention, much less an expression of support, for fiduciary principles.

Two primary observations stand out. First, these associations are unambiguously reluctant to embrace fiduciary procedures that support a fiduciary standard. While there are expressions of *conceptual* support for fiduciary responsibilities, there is no expression of *operational* support for code language defining fiduciary procedures (such as those within the Uniform Prudent Investor Act, or offered elsewhere). Instead, associations recommend the Commission either adopt its own association code, or adopt language allowing “flexibility” for member firms to “tailor their codes of ethics to accommodate their (own) .. business activity.” Second, opposing adoption of specific fiduciary procedures is supporting the current regulatory framework, where firms and associations already write their own codes.

Leading Financial Planners

In contrast to these views, are the views of many leading financial planners. These leaders strongly urge investment advisors embrace their fiduciary responsibility. Their sentiments are expressed in numerous forums, one being a recent book on best practices of financial advisors. (a) A sampling of these views are telling:

“This will be a short chapter. You are a fiduciary. That’s it. End of chapter.”
-- Andy Hudick, Roanoke, Virginia

“The way I feel about my clients, I am embracing the fiduciary role.”
-- Barbara Pope, Chicago, Ill

“Planners are fiduciaries whether they like it or not, because they get to know clients, and then offer investment advice tailored to specific situations...”
-- James Wilson, Columbia, SC

Based on this research, Deena Katz believes its clear that planners are Fiduciaries. If the law doesn’t say it now, it soon will.”
-- Deena Katz, Coral Gables, Florida

“We say we are fiduciaries. People say that we are handing people a loaded gun, but we don’t think so.”
-- John Blankinship, Del Mar, California

“If you don’t want to accept fiduciary responsibilities, get out of financial planning. Financial planning is just now on the cusp of becoming a real profession ... Planners at the top of the profession accept the label without comment.”
-- Mary Rowland, Best Practices for Financial Advisors

Conclusions

We urge the Commission seek further comment in light of the above-noted views from leading associations and financial advisors. First, we urge the Commission to seek comment from leading financial advisors on the procedures that should be part of an SEC Code of Ethics. Second, we urge the Commission to seek additional comment on the following questions from the associations mentioned above:

1. It appears your organization opposes a code of ethics that explicitly embraces fiduciary procedures and standards. If this is correct, please explain why your organization believes your members should not follow fiduciary procedures. If this is incorrect, please describe the procedures your organization supports to uphold fiduciary standards.
2. Some advisers say they are fiduciaries *some of the time*; other's, like FPA Chair, David Yeske, believe an adviser should "think and act like a fiduciary at all times." If your view is that an adviser is not required to be a fiduciary at all times, under what circum-stances do you believe an adviser may discard its fiduciary standards? Also, what obligation does an adviser have to disclose to clients when fiduciary standards have been discarded?
3. Some experts believe adherence to fiduciary standards would increase with an understanding of fiduciary procedures. What grade (A – F) would you give your membership on this subject? What grade would you give your membership on *wanting to learn* this subject?
4. Chairman Donaldson notes fiduciary breaches are linked to the recent scandals. If he's correct, would your association protect its' reputation by helping members learn and adhere to a code of fiduciary procedures that distinguish them from lesser qualified intermediaries? Would your association support a code of fiduciary procedures if your members were allowed a significant phase-in transition time?

Chairman Donaldson has articulated why a fiduciary standard is important, and is correct in seeking a code that reflects such a high standard. Yet, this standard will only be adhered to if the Commission explains what the standard means. In light of the current scandals, an SEC Code offering advisers guidance in defining a fiduciary is particularly timely. Investors and the vast majority of stakeholders will applaud such a standard. We urge the Commission to request additional comment we believe will support a Code based on defined fiduciary procedures and oppose a Code that requires anything less.

Thank you for this opportunity to offer these recommendations. We would be pleased to answer any questions.

Sincerely

Donald M. Rembert/Kar

Donald M. Rembert
President & CEO
Rembert D'Orazio & Fox
703/821-6655

Knut A. Rostad

Knut A. Rostad
Knut A. Rostad Associates
301/320-9180