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United States Senate

WASHINGTON, DC 20510-4402

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January 8, 2004

Mr. William H. Donaldson
Chairman
U.S. Securities and Exchange Commission
450 Fifth Street NW
Washington, D.C. 20549

Dear Mr. Donaldson:

Enclosed please find a copy of correspondence from one of my constituents, Mr. Bill Good. I would appreciate your review and response to his comments.

Please forward your response to Jenny George of my Washington D.C. staff. Thank you for your attention to this matter.

Sincerely,

Orrin Hatch

Orrin G. Hatch
United States Senator

OGH:jgg

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December 8, 2003

The Honorable Senator Orrin G. Hatch
United States Senate
104 Senate Hart Office Building
Washington, DC 20510

Dear Senator:

By way of reminder, you were a keynote speaker at a conference my company presented in Washington a few years ago.

I am writing to urge you to take a look at the dreadful solution the SEC is now proposing for the awful mess in the mutual fund industry.

When a solution to a problem makes the original problem worse, a new solution should be proposed.

I am enclosing an article by Lou Harvey, Chairman of Dalbar, Inc., a market research firm specializing in the financial services industry.

In this article, he shows:

1) It will do no good to force after-hours processing into the pre-4:00 PM time frame, since insiders will continue to have the opportunity to do late trading and market timing. It also takes away selling time since orders will have to stop around noon to allow time for processing, thus putting the small investor at an even greater disadvantage.

2) The cost and chaos this will cause from the point of sale to the back office is enormous. New systems and procedures will affect everyone that touches a mutual fund order. Investors will end up paying tens of millions for this.

3) Once per day pricing was created in 1940 when we did not have computers to handle continuous pricing as occurs with stocks and bonds. Continuous pricing is the proven practical alternative since there is no opportunity for arbitrage. I urge you to take a look at this article.

I have sent copies of this article to 2000 of my clients and urged them to contact their Senators, Congressmen, the SEC and NASD. If I can be of any further assistance in this matter, please have one of your staff call.

Sincerely,

Bill Good

Bill Good
Chairman

DALBAR
The Measurement of Success

THE FOUR O'CLOCK SHUFFLE

by

LOUIS S. HARVEY
CHAIRMAN
DALBAR, INC

December 5, 2003

The 2003 mutual fund scandals have triggered an avalanche of attention on enforcing the 4:00 PM cutoff for mutual funds to accept transactions. Unfortunately, enforcing the 4:00 PM cutoff will do absolutely nothing to curb wrongdoing by mutual funds or the insiders that profit at the expense of long-term investors.

This analysis examines the intent of the 4:00 PM cutoff, the unintended consequences, and identifies the winners and losers. The recommendation provides a rational solution that offers real protection to investors.

INTENT OF 4:00 PM CUTOFF

The unproven theory of the advocates of rigorous enforcement of the 4:00 PM cutoff is that this will remove the opportunity for insiders to insert transactions after the close of business that takes advantage of market moving news that occurs after 4:00. By doing this, the news that occurs after 4:00 PM is reflected in the next day's price, thus removing the advantage.

WHAT'S WRONG WITH THIS?

Rigorous enforcement of the 4:00 PM cutoff simply transfers the problem to another time of day. As a matter of fact, it transfers the problem to a time of day when there is even more opportunity for mischief.

If, as advocates propose, mutual funds can only give the current price to transactions that are received before 4:00 PM, then sellers of mutual funds must establish an earlier cutoff to do the processing required to meet the deadline. In today's world this processing takes up to four hours to complete, which would translate to a 12:00 Noon cutoff for sellers.

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The 12:00 Noon cutoff would mean that average retail investors could not buy or sell after 12:00 o'clock but insiders would still have four hours to react to afternoon news. News such as Federal Reserve policy statements and rate changes which occur at 2:00 PM.

This cure is more damaging than the disease.

UNINTENDED CONSEQUENCES

In addition to the fact that this proposal will make a bad situation worse there are some unintended consequences that should be considered.

The operational implications are that existing systems and controls will have to be scrapped and replaced with new ones in every firm that sells mutual funds, every record keeping firm, every employer that makes employee payroll deductions for retirement plans in mutual funds, and every mutual fund company. The scale of this is in the tens of thousands of companies.

This widespread revamping of systems will undoubtedly lead to:

- Large Scale Changes: The 4:00 PM cutoff will not only affect mutual fund systems but also every broker/dealer, record keeper, annuity company, and employer will have to create new systems.
- Mischief & abuse: From unscrupulous systems builders that seek to capitalize on the chaos this will cause.
- Blackout periods: As firms switch from old systems to new systems.
- Loss of control: Since the controls for the new systems will not have the advantage of the test of time.
- Delays: These are inherent in a massive effort such as this.
- Errors: Invariable errors will occur when hundreds of programmers are required to write complex systems in a short time and millions of people are retrained to use them.
- High costs: The cost of replacing existing systems is enormous since new computers and networks must be put in place at the same time that the old ones continue to serve the public.
- Increased Manual Orders: Since fund companies will be open for business until 4:00 but the seller's cutoff must be earlier, sellers will bypass the regular system and telephone orders into fund companies, resulting in higher costs.

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- Increase Internet Usage: Sellers that are able will make use of the Internet to place trades which will provide increased efficiency over manually entered orders.
- Limit Twenty-four Hour Trading: When this is implemented it will render the 4:00 PM cutoff obsolete.

WINNERS & LOSERS

The proposed 4:00 PM cutoff and its massive implications will produce payoffs for some at the expense of others. The most predictable examples are:

Winners

Technology Companies that will receive orders for hundreds of millions of dollars in computers.

Programmers & other technical staff required to design, test and implement the new systems.

Insiders will have even greater opportunity to benefit at the expense of the small investor.

Losers

Small Investors who will have a shortened trading window due to earlier cutoffs.

Mutual Fund Shareholders will pay hundreds of millions of dollars for the cost of the change in the form of higher expenses.

Sellers of mutual funds (brokerage firms, employers, etc.) that will not be able to pass their cost on to others.

Unaffected

Mutual Fund Companies will justifiably pass the cost to shareholders in the form of higher expenses.

Record Keeping firms that will pass the cost of the change to the institutions that are their customers.

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RECOMMENDATION

The mutual fund problems of late trading and market timing arise from the fact that there is a daily cutoff, regardless of the time. Unlike stocks, bonds or commodities, which are continuously being priced, mutual funds' once per day pricing creates opportunities for wrongdoing. As soon as the price is set, it is immediately stale so late and last minute traders have an opportunity to arbitrage.

In 1940, when this daily pricing system was codified into law, computers were primitive and the concept of continuous pricing of mutual funds was impractical.

In 2003, continuous pricing is very practical and could be done at a fraction of the cost of enforcing a 4:00 PM cutoff. The changes would require revamping portfolio accounting systems that compute the prices. This would limit the impact to mutual fund companies and cost investors a fraction of the 4:00 PM cutoff.

The continuous pricing of mutual funds would eliminate the profit from late trading and market timing and protect the small investor from insider's predatory practices.

Additionally, continuous pricing of mutual funds will prepare the mutual fund industry for the eventuality of 24 hour per day trading.

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