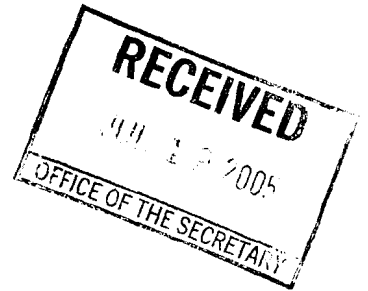


Jonathan G. Katz, Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

July 18, 2005

Re: File No. SR-NASD-00-23
Proposed Rule Change and Amendment No. 2 by the NASD
Relating to Amendments to Order Audit Trail System Rules



To the Commission:

This letter comments on the provision for small firm exemptive relief - Rule 6955(d) - of the above referenced Proposal. We have previously commented on this provision by letters dated March 26, 2001 and April 26, 2000, and on the OATS rules in general by letter dated June 6, 2000 addressed to the NASD.

We are a small, family-owned self-clearing broker-dealer, in business since 1961. This firm qualifies for a temporary exemption from OATS as the Rule is currently proposed (provided that we terminate a clearing relationship with another small firm, which we are willing to do). However, we remain deeply troubled by the limited nature of the NASD's authority under the exemption provision. In our past correspondence, we have explained that there is no cost-effective means by which this firm could fully comply with OATS, rendering this Rule effectively a death sentence for the firm. Since our last correspondence on this matter in March 2001, market conditions have changed so as to make this statement even more imperative. Because of these changed conditions -- coupled with the extreme seriousness and burden of OATS -- we are stating these concerns once again.

In our first letter on OATS dated June 6, 2000, a copy of which is attached, we noted that OATS disproportionately impacts certain firms. Specifically, this includes any small or low volume firm (because automated system applications enjoy enormous economies of scale) and firms that use a large number of limit orders (because OATS functions as a tax on orders, increasing their cost regardless of whether they result in executions). That letter included a specific example of how a typical investment decision at this firm (involving several bunched clients and a series of scheduled limit orders) would result in 74 order entries to potentially obtain four executions, each of which had only a 40% chance of occurring. Based on the fact that every OATS report includes many fields of data including a 12 digit time code, we concluded that OATS would not simply increase our costs of execution and clearing -- it would multiply those costs.

Since that letter was written, however, the situation has gotten far worse. That letter assumed that four executions, if obtained, would result in only four execution reports. Since 2001, we have seen the adoption of decimalization and full ascendency of ECNs in control of the Nasdaq market. As a result of these changes, we now regularly receive multiple partial executions even on small orders. Indeed, it is no longer exceptional to receive ten small executions to complete a single 500 share trade. Accordingly, in the example cited above, we could add an additional forty execution reports (each and every one with the possibility of problems or errors). This development underscores and confirms our belief that it is essentially impossible to deal with OATS reporting on a manual basis within the contours of this firm (we retain exactly three employees). Such reporting would only make sense in a fully automated computer-based system. Unfortunately, the developers of those systems do not, to my knowledge – and are unlikely to – focus on the needs of small, low volume firms. Thus, our difficulty with OATS does not stem from a lack of adequate time to engage in preparation or planning. The rule is simply not compatible, in our judgment, with the business of this firm, and very likely that of the other small firms to which exemptive relief has been properly targeted.

Against this backdrop, we continue to believe that the current exemption provision is unduly tentative and fragile. Particularly troubling is the fact that exemptive authority will expire in five years. As explained above, under current conditions, OATS is not an appropriate regulatory solution for the industry's smallest self-clearing firms. The NASD presumably agrees with this or the exemption provision would not exist. Should conditions change, the burden should be on the NASD – not on a handful of very small private companies – to make a public case for broader application. In addition, the current requirement regarding disciplinary history – essentially requiring a perfect record – is inconsistent with serious ongoing small firm relief. No firm can maintain a perfect disciplinary record forever. We understand the purpose of this requirement (and agree with it) but without some exceptions or allowance of discretion, this requirement if continued indefinitely would eventually nullify the entire exemption provision.

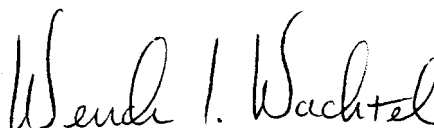
In recent years, the SEC and NASD have given substantial attention and support to matters particularly affecting small firms. We greatly appreciate this important trend. In addition, we understand that the NASD, as stated in the proposal under discussion, wishes to engage in further study before finalizing the small firm exemption from OATS. We have great respect for and confidence in that process.

Thank you for giving these comments your serious consideration. Please feel free to contact us for any further discussion.

Sincerely,



Bonnie K. Wachtel, CEO



Wendie L. Wachtel, COO

Richard G. Ketchum
President & Chief Operating Officer
National Assn. of Securities Dealers, Inc.
1735 K Street, NW
Washington, DC 20006

January 6, 2000

Dear Mr. Ketchum:

This will follow-up on our discussion at the NASD forum last month regarding the urgent need for an extension of the deadline for implementation of OATS Phase III so that small firm exemptions and alternative compliance methods can be considered. We have completed analysis of the OATS Rules ("OATS"), recent interpretations, and software products currently available on the market in conjunction with our business. We conclude that OATS threatens the well-being of our customers and the economic viability of this firm.

As is further described below, we believe the cost of OATS is proportionately greatest for firms that (1) have a small revenue base (particulary self-clearing firms); (2) are very efficient in their use of personnel; (3) rely heavily on Nasdaq securities; and (4) extensively use limit orders. Because our firm is perhaps the smallest and most efficient in the country (we run a full service, self-clearing firm with a full-time staff of three); relies heavily on Nasdaq and makes extensive use of limit orders to effect our investment strategy, we would perhaps experience a greater proportionate cost from OATS than any other firm in the industry. This is a strange result indeed for a firm that is not and never has been a Nasdaq market-maker (we were the victims of any abuses from those firms), and which has never -- in forty years of operation -- experienced a serious customer complaint.

Further consideration is all the more warranted because there are many established alternative methods under which the purposes of OATS can be met. Indeed, we know of no other rule in place from the SEC, IRS or any other regulatory body in which use of expensive technology -- mandated strictly for regulatory purposes -- does not include alternatives for small firms. These would include use of client waivers, strict requirements for order handling personnel, submission of data on hard copy and others. Good regulatory practice requires special consideration for small firms, so as not to force consolidation in the industry -- and thereby hurt owners and limit customer choice -- without compelling justification.

Further, were there not many other reasons for taking special account of the effect on small firms, we note that this category will disproportionately include firms owned and managed by minorities and women. Wachtel & Co., Inc. is such a firm.

Finally, we realize that OATS was initially made open for comment some time ago. However, the rules are extremely technical and burdensome to analyze, and in our opinion, well beyond the comment writing capacities of the principals of most small firms (without use of expensive outside counsel). Moreover, as a practical matter, it would have been simply impossible to analyze the cost of OATS without knowledge of relevant commercial software, which has only been produced recently. The vendors of this software inform us most Phase III firms have done nothing to assure compliance with OATS. There is plenty of time to delay and study the true costs and alternatives -- the type of consideration good regulatory practice requires.

About Wachtel & Co., Inc.

This firm was founded in 1961 by Sidney and Irma Wachtel, and is currently managed by daughters Wendie and Bonnie. Sid (now largely retired) is a former economist with the US Treasury, a General Securities Principal and Financial Principal, and former Chairman of the local NASD District Business Conduct Committee. Wendie is a General Securities Principal and Financial Principal, and has formerly served as Vice-Chairman of the local NASD Business Conduct Committee. She has also served as president of the Security Traders of Washington, a member of the Uniform Practice Committee, a regular Securities Arbitrator, a Nasdaq Qualification Panel Member, and consultant for the Financial Services Volunteer Corps assisting in establishing capital markets in Eastern Europe. Bonnie holds an MBA in Finance, is an attorney, and a Certified Financial Analyst. She is a General Securities Principal, former Vice-Chairman of the District 9 Business Conduct Committee, has served as a director of several public companies and is widely experienced as a securities arbitrator in several forums. Wendie and Bonnie collectively have more than 45 years experience in the securities industry.

The firm is principally a retail full-service business, including limited investment banking and market-making in a few (generally inactive) Bulletin Board stocks. There are about 300 active accounts, 50-100 of which are discretionary. This is a low volume operation; we do not advertise and rely for our business on client retention, word of mouth and reputation for honesty, skill and good judgment. Annual commission revenues are probably less than one medium grade producer at Merrill Lynch. They are also extremely erratic, with daily trades varying in number from

fifty to zero. We are extremely concious of maintaining good practices from the point of view of both regulatory compliance and customer satisfaction. While no firm in this industry has a perfect record of compliance, ours is close to perfect. In addition, in forty years of operation -- all of which featured involvment, to some degree, with smaller speculative stocks -- we have never been named in litigation or arbitration, have never paid a settlement, and indeed, have never experienced, in any form whatsoever, a serious customer complaint. This is a direct result of the hands-on, continuous supervision and control of every account and every trade by a member of the Wachtel family.

For puposes of OATS, two facts should be emphasized. This firm has a full-time staff of exactly three people: Wendie, Bonnie and a back-office cashier. Every order on the trading desk is personally handled from start to finish by either Wendie or Bonnie.

The Cost of OATS

As a preliminary matter, it is important to clarify the distinctive effect of OATS on low versus high volume firms. Our firm uses a paper ticket system in which orders are created, sent to the trading desk, time stamped on execution, then carried to the back office for processing at the end of the day. Most of the difficulties we describe below would not be incurred if our firm -- as several large firms -- used a seamless automated system where orders are entered and routed and, following execution, delivered to the back office, all via computer without use of paper in any form. However, such a system is completely cost prohibitive for a firm of our size. We will have to maintain paper tickets for processing executed trades regardless of record keeping for OATS. Viewed in this light, it is obvious that imposition of OATS on a manual system requires recording virtually all order information at least twice. It is thereby duplicative, inefficient and -- worst of all -- extremely prone to error. The key point is that a firm's central processing mechanism is largely an overhead cost. It does not vary on a per trade basis, and thereby hits hardest on low volume firms. This is why we conclude that OATS, if not reformed, distorts competition in the industry, potentially kills small firms and robs customers of the opportunity to work with the firm of their choice.

Effect on Market Orders

For our firm, OATS effect on market orders is oppressive, and its effect on limit orders is devastating. We describe the two situations below.

About 5% of our order flow is called in by a few part-time reps. The balance is divided between orders called in directly by clients, and those generated by the Wachtels for clients we advise. Client directed orders tend to be market orders, whereas orders generated by the Wachtels are usually placed on a limit.

Under our current system, market orders are generally called in by clients directly to the trading desk. Simple orders are executed while the client remains on hold. All marketable orders are routed immediately; we certainly have no incentive to do otherwise, and executions are monitored against the market directly by Wendie or Bonnie. We believe our service is as fast or faster than any service offered by an order entry firm. Were it otherwise, our clients have plenty of alternatives elsewhere -- this is probably the most competitive industry in the world.

Under OATS, there are basically two alternatives for compliance. One is to enter the order receipt and routing information prior to transmitting the order. If the firm can use software with an embedded clock, this has the advantage of obviating the need to type in a twelve character time code, the most oppressive feature of OATS. However, this mechanism has several drawbacks. First is the fact that it delays execution of an order for several seconds at a point when seconds are at a premium. We estimate that our manual ticket system creates no delay in execution because the order can be written approximately as quickly as the client can speak. Typing an order in OATS, without the time but including the identifier and all of the appropriate codes, we estimate at approximately 20 seconds. The full impact of this inefficiency, however, can only be understood in connection with multiple orders. Suppose, for example, a client calls in four market orders together, all in Nasdaq stocks. Under the current system, it's likely these orders can all be called into one market maker, probably resulting in executions on all of them within a minute of placing the client on hold. Under OATS, however, this is not possible. If all of the orders are first entered into OATS before calling the market-maker, the system will show different receipt and routing times for each one, which is not accurate. The alternative is for the orders to be processed one at a time -- write the ticket, type into OATS, call the market maker, execute. By the time this process is finished for the last order, we estimate about 4 minutes will have passed from the time the client obtained his "current quote." Were I a client, I would consider this an interference with best execution -- at least in comparison with the system available now.

The alternative to this system (which, as indicated above, is virtually required for multiple orders) is to execute the orders immediately, then later enter data into OATS. Consideration of this alternative illustrates the unintentional yet devastating attack OATS entails on extremely efficient firms such as ours.

The authors of these rules apparently believe (and I paraphrase) that "business can continue normally" because "the OATS data can be entered simultaneously with the trade or at a convenient time during the day." Excuse us, but we beg to differ. If the 12 character time codes must be entered manually, OATS is simply an avalanche of clerical work. There is no convenient time to do such work, and no one available to do it. Unlike at larger firms, there is no full-time person sitting at the trading desk, available to do menial tasks during slack times. All orders are handled by Wendie and Bonnie. When trading volume is down, we are employed in the many other tasks necessary to run this firm. Chief among them is investment research, a necessary task for the many clients who rely on us for judgment and skill. Pulling us away from this task for the purpose of voluminous data entry is just about the worst trade-off from the stand-point of client well-being that we could imagine.

Further, it is no answer to this problem to suggest that we hire additional personnel. In the first place, we have no need for such hiring apart from OATS. In the second, an OATS related position would be impossible to fill, since many days would involve no work at all, while others would require work on an unsupervised night shift (with heaven knows what type of security implications). Moreover, as a more general matter, in our experience hiring employees is never an answer to regulatory problems. To the contrary, employees create problems through errors and inexperience, leading to the ever-burgeoning literature on systems of supervision. The longevity of this firm, its client loyalty and lack of regulatory problems are all due to one key fact -- hands on operation of virtually every aspect of the business by members of the Wachtel family.

Just to emphasize -- none of the regulatory problems that gave rise to OATS were created by highly controlled small firms such as ours. Virtually all such problems were the result of bad actors or bad practices at large firms. These firms have lots of clerical personnel and lots of profit to fund automated systems -- driven by advertising, hiring salesman and aggressive trading. We have nothing against large firms, but respectfully demand that our business model be recognized. We are very sensitive to cost because we have no desire to increase our revenue. Our business model is not broken -- it is just incompatible with a huge regulatory burden like OATS.

OATS Effect on Limit Orders

The above discussion concerns client-directed market orders. However, the reputation of this firm, most of its business and its reason for being is tied to the investment approach and recommendations of the Wachtel family. We have two principal specialties: (1) relatively obscure, thinly traded or early stage firms; and (2) a contrarian approach to mainstream investments.

In both cases, the use of limit orders is absolutely central to our approach. We tend to purchase stocks that are declining, and rarely do we place a buy order for any security without several more orders, at lower prices, being developed or entered at the same time. The same multiple order approach is used when shares are sold.

In our current system, a typical order will consist of perhaps ten bunched clients, including five discretionary orders and five with discretion as to price ("DATP"). Orders placed with DATP are generally on an instruction along the lines that shares should be bought or sold if Wendie or Bonnie choose to take a position for themselves or other clients. Because of the grant of discretion, these orders do not represent a final decision by either the broker or client to purchase any given stock. However, the entire process is virtually costless, since it only involves a quick notation of the time and date of the conversation. When a decision is made to purchase, bunched orders are placed with a market maker (frequently two or three at a time, with different price limits). Through this process of extremely efficient order handling, we are able to provide sophisticated account management even to relatively small clients.

Now consider the same process with the costs imposed by OATS. Begin with the initial discussion with the nondiscretionary client. Assume, as is often the case, that six stocks will be approved with the expectation that only three will be chosen for purchase. Nevertheless, an "order received" entry must be placed on each of the six stocks -- for five clients, 30 entries. Add in the orders for discretionary clients (which under OATS, are treated as one order) and assume that three bunched orders (at different price limits) are placed on three stocks. This will entail nine entries for order received and nine for routing, a total of 18 entries. Also assume that one of the DATP clients cancels before the top order is executed -- add 24 additional entries (15 to cancel, 9 to reroute). Finally, assume the price limit is changed on the highest limit on one of the stocks to adapt to market conditions; add two more reports. The result: 74 OATS reports to place nine orders, which collectively have approximately a 40% chance of being executed. Put differently, to achieve four executions, the OATS system required an average of eighteen entries per trade -- adding up to hundreds of reports in a day -- every one of which contains the possibility of a time exploding error. Furthermore, every particle of this monumental cost is superfluous to and duplicative of our extremely effective current system.

We realize that it may be considered unusual for a client to place three orders at a time on each stock or to change price limits on a regular basis. We agree. We have deliberately chosen to employ this contra-market system on the basis of our

experience and professional judgment. We also note that this approach is extremely beneficial to the market as a whole. These are exactly the type of orders that add stability in escalating or collapsing markets.

Finally, we realize there are means by which we can avoid some of the cost of OATS, and this may be the most disturbing feature of the rule. We can choose listed or Bulletin Board stocks instead of those traded on Nasdaq (thereby avoiding stocks that we believe are the most attractive for our clients); or we could not enter those limit orders that are farthest from the market (potentially resulting in a devastating "miss" of a desired execution because an order was not in place in a fast moving market). In other words, the OATS system creates costs so oppressive that it virtually mandates that we diminish the service and value we provide to clients. Although we do not doubt the good intentions of the regulators, we can hardly express our frustration with this unwitting interference with our clients' best interests.

In summary -- the OATS system vastly multiplies for us the cost of handling market orders; we estimate by a factor of 10. For limit orders -- in view of the chilling effect towards even placing those orders -- the cost of the system is limitless.

Alternative Compliance Approaches

We have attempted to frame our discussion of OATS within a cost/benefit analysis. The prior discussion focused on cost; we now turn to the regulatory purpose of OATS and alternative methods of achieving those benefits.

Unfortunately, we are hampered in this regard by the fact that the SEC and the NASD have not chosen to articulate with particularity the regulatory purpose of OATS. We read that it will provide "a better picture" of the path of orders through the system, but this statement does not attempt to justify the rule's enormous cost. We look forward to speaking with representatives of the SEC and NASD to better understand OATS' intended benefits. This will help us sharpen our analysis and suggestions.

In the meantime, however, we note there is widespread precedent in every regulatory system we know of for exemptions for small firms and individuals from expensive and burdensome regulations. A small sample includes the following: all employment discrimination statutes exempt firms with 15 employees or less; IRS has cut-offs based on size for the mechanism and timing of payroll and other tax reporting; the securities industry has "grandfathered" a variety of individuals from training and testing obligations; both the SEC and the NASD provide exemptions from mandatory "blue sheet" reporting through electronic means.

Alan Greenspan himself has noted that a "one size fits all" approach to regulating financial institutions is inefficient and should be avoided.

Applying these precedents to OATS yields many possibilities for alternative methods of compliance. These include:

(1) Exempt Order-Entry Firms. If the SEC is most concerned with the practices of market-makers (as alleged in the price-fixing lawsuit), firms that do not make Nasdaq markets should be exempt. At a very minimum, only the routing function for such firms should be reported, because it is the only function that has direct contact with the market-maker.

(2) Require strict standards for Order Handling Personnel. If the SEC is concerned with mishandling of orders, or "bad actors," requirements for individuals on the trading desk should alleviate that concern. One possible suggestion is that every individual on the trading desk (not just the supervisors) have been qualified as a firm principal for a period of years. This solution is particularly appealing because it keeps the regulators neutral in choosing various business models for firms in the securities industry. Some small firms can justify the cost of OATS as a compliance measure because they use inexperienced clerks on the trading desk. Firms like ours have already invested in our people for compliance, and therefore do not require electronic surveillance.

(3) Client Waivers. If the SEC is primarily concerned with client protection, we believe the drafting of a client waiver would be an excellent opportunity for the regulators to fully articulate the benefits of OATS. We will circulate the waivers to our clients; anyone choosing not to sign will be required to transfer out. Again, we believe this is a perfectly appropriate grounds for an exemption. Many clients of brokerage firms may derive an extra measure of confidence from electronic regulatory surveillance. We do not believe that is true of our clients. Our bond with them is their trust and confidence in our services, a bond we have invested many years to develop.

(4) Exemption of Small Self-Clearing Firms. If the SEC is primarily concerned that firms only be exempted where the cost is prohibitive, and that no incentive be created for larger firms to break up for the purpose of avoiding OATS, limit the exemption to self-clearing firms. This is justified on the grounds that small introducing firms will obtain some measure of OATS support from their clearing firm. Also, the regulators can be assured that self-clearing will never come back as an industry trend. For most firms, it would be far more expensive than OATS.

(5) Use of Paper Filing. While all of OATS is burdensome, we are less concerned with collecting the required information than with its electronic transmission. Filing on paper, through a means that does not require duplicate recording, would be far more efficient for firms that otherwise use a paper system. If the NASD does not have a means of storing the records, they could be sent to the firm's CPA.

(6) Individual Application. Finally, as a last resort, the NASD could grant waivers by individual application based on the factors cited above.

These suggested grounds for exemption could be used alone or in combination, and in combination with firm size. For purposes of our firm, we would gladly embrace an exemption entailing all of the requirements listed above.

Conclusion

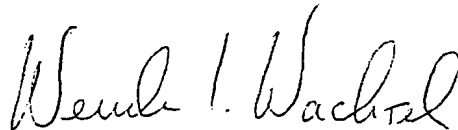
We fully understand the difficulty and importance of regulating the securities markets. We also understand how lack of regulatory diligence by the NASD could lead the SEC to call for a mechanism for greater surveillance. However, oppressive regulation that ignores traditional protection for small firms, hits hardest on those firms that were not involved in any way in regulatory nonfeasance, and that threatens a forty year old family-owned business with no client problems, is certainly not the answer. At the very least, the SEC should delay implementation of Phase III and study the true costs of this system on the industry's smallest firms. Further, to the extent that any formal analysis of these competitive issues has been undertaken, we request a copy of that analysis.

Again, we do not question the good intentions of any regulator who has advocated implementation of OATS. But as the rules stand, this system threatens to destroy our firm with no discernable benefit to our clients. We look forward to discussing these issues in person at your earliest convenience.

Sincerely yours,



Bonnie K. Wachtel, CEO



Wendie L. Wachtel, COO