7 August 2018

Brent J. Fields, Esq.
Secretary,
Securities and Exchange Commission
100 F Street, NE,
Washington, DC 20549-1090

Delivery by Commercial Courier
and
Email: rule-comments@sec.gov

Re: File Number S7-07-18
SEC Release No. 34-83062 – "Regulation Best Interest" Proposed Rule
Industry Member Comment Letter to "Regulation Best Interest" Proposed Rule

Dear Mr. Fields:

This Comment Letter is being timely filed with the Securities and Exchange Commission (SEC) in response to certain proposed amendments identified in the SEC "Regulation Best Interest" proposed rule.

The "Regulation Best Interest" proposed rule identifies desirable amendments for establishing a standard conduct for broker/dealers (hereafter, "Firms") and their natural persons associated with them as registered representatives (hereafter, "brokers") when making a recommendation of any securities transaction or investment strategy involving securities to a retail customer. This standard of conduct, as proposed by the SEC, will require Firms and their brokers to act in the best interest of the retail customer at the time a recommendation is made without placing financial or other interests of the Firm or the broker ahead of the retail customer.

This Comment Letter's analysis will limit itself to addressing the following two (2) questions posed by the SEC, in the "Request for Comment on Proposed Care Obligation" section in SEC Release No. 34-83062 – the "Regulation Best Interest" Proposed Rule:

1. "Under the Care Obligation, a broker-dealer [the Firm] must exercise reasonable diligence, care, skill, and prudence when making a recommendation, including assessing the potential risks and rewards associated with the recommendation. *Do commenters believe that Regulation Best Interest is sufficiently clear that a broker-dealer [the Firm] and its associated natural persons [brokers] may make a recommendation which my result in investor losses due to market or other risks inherent in investing*?"[1] (Emphasis supplied)

2. "Do commenters agree that turnover rate, cost-to-equity ratio and in-and-out trading are relevant factors for determining that a series of recommended transactions is excessive for purposes of paragraph (a)(2)(i)(C)? *If not, what factors should a broker-dealer [the Firm] consider with respect to this proposed obligation?* Should the Commission expressly articulate the relevant factors as part of the rule?[2] (Emphasis supplied)

[1] SEC Release No. 34-83062 – "Regulation Best Interest" Proposed Rule at p. 161.

[2] SEC Release No. 34-83062 – "Regulation Best Interest" Proposed Rule at p. 165.



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This Comment Letter will *collectively* address the *italicized* portions of *both* "Request for Comment" questions set forth above as posed by the SEC, identifying (1) where this Industry Member finds agreement with the "Regulation Best Interest" proposed rule; (2) where or in what scenario the "Regulation Best Interest" proposed rule works a natural inequity in the overall justice of the rule and *why* an exception or exceptions should be made to the "Regulation Best Interest" proposed rule; and (3) how this natural inequity or deficiency might be remedied.

With this perspective in mind, Network 1 Financial Securities – your Industry Member registered with the Commission and member of the Financial Industry Regulatory Authority (FINRA) – expresses sincere appreciation for this opportunity to respond to the proposals set forth in SEC Release No. 34-83062. Network 1 Financial Securities is an industry member that has been engaged primarily in investment banking and secondarily in securities brokerage, including market making and trading, since 1983.

## 1. General Agreement with the "Regulation Best Interest" Rule, as Proposed

The essence of the "Regulation Best Interest" Rule, as proposed, comes down to this: When offering a particular security, the broker must conduct due diligence on the security that he is recommending to a customer; this due diligence should enable the broker to understand all the "bells and whistles" of the securities product that he intending to recommend to his customer; and, on the basis of this due diligence and understanding of the product, the broker must have formed a reasonable basis to believe that the particular security that he is contemplating recommending to his customer is "in the best interest of at least *some* retail customers" and, equally important, that this particular security is "in the best interest of *this* retail customer", whom the broker should know fairly well as a result of informing himself about the customer's traditional suitability KYC criteria; but, in addition to this, the broker should include in his suitability analysis, consideration of the "costs" associated with this particular security, as well as "liquidity, risks and potential benefits, volatility, likely performance of market and economic conditions, the expected return of the security or investment strategy, as well as any financial incentives to recommend the security or investment strategy."[3] Finally, in order for this recommendation of *this* security to *this* customer to be deemed to be "in the best interest of the retail customer", the broker must be able to successfully defend against a regulatory body's charge that commission dollars – that is, the financial interests of the Firm and the broker – are not the motivating factor, primary or otherwise, that drives the broker's recommendation to the retail customer. In addition, no longer would it be a defense for the Firm or the broker to claim that this particular recommendation – this transaction – is suitable standing on its own; instead, now the transaction must be in the best interests of the retail customer in view of the entire series of transactions in the retail customer's portfolio.

This makes perfect sense when the broker is selling investment company securities (such as, mutual funds, variable life insurance, and variable annuities) and that entire panoply of securities products that were once considered exotic but today are considered commonplace.

This "Regulation Best Interest" proposal makes sense when a broker replaces one variable life insurance policy that is, hypothetically speaking, in its third year of its contingent deferred sales load (CDSL) for a different variable life policy on the pretext that the replacing policy has a "better" rider – however "better" may be explained by the broker. Ultimately, the "devil is in the details" and the replacement policy may indeed be justified; but the point, here, is that in the context of replacement of variable life policies – and similarly, replacement of variable annuities – the application of a "Regulation Best Interest" standard can make sense.



[3] SEC Release No. 34-83062 – "Regulation Best Interest" Proposed Rule at pp. 137-139.

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The same conclusion can be reached for the many various scenarios involving broker justification for selling one mutual fund to a retail customer and, within a short period of time, selling a second or third or more mutual fund(s) that is/are either identical to or similar in all or most material aspects of the first mutual fund – especially when the first mutual fund is still in its early CDSL stages. Again, the "devil is in the details" and the additional purchase and/or replacement fund(s) may indeed be justified; but the point, again, is that the selling and/or replacement of mutual funds having identical or nearly identical qualities to a retail customer would seem to justify the operation of a "Regulation Best Interest" standard.

This "makes sense" conclusion about the "Regulation Best Interest" proposal, especially as relates to mutual funds, variable life insurance, variable annuities and that entire panoply of securities products that were once considered exotic but are now considered commonplace, is further justified by the explosion of financial services designations that are intended to "serve as external validation of expertise" in the financial services industry.[4]

In the "old days", insurance agents were just insurance agents – individuals who sold fixed insurance and not securities; and, stockbrokers were simply traditional Wall Street stockbrokers[5] – individuals who sold, well,

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[4] *See* Global Alphabet Soup: Internationally Recognized Professional Designations in Finance, Journal of Financial Education, 38 (3/4), Fall/Winter 2012.
https://www.researchgate.net/publication/258033927_Global_Alphabet_Soup_Internationally_Recognized_Professional_Designations_in_Finance

[5] *See* William O. Douglas and George E. Bates, Stock "Brokers" as Agents and Dealers, 43 Yale Law Journal, Issue 1, Article 12 at 59: "Ordinarily stockbrokers are agents working for a commission. They attend to the purchase and sale of stocks or shares or other securities for and on behalf of clients. They are employed to buy and sell shares of stock of incorporated companies by their principals. It cannot be said that a person who buys for himself and sells to another is acting as a stockbroker for that other. Stockbrokers, on the other hand, do not transact business for themselves, but for others. Their employment is to buy or sell stocks, and they receive compensation for their services. They act as agents of the persons for whom the purchases or sales are made. Their interest in the transaction is only to the extent of the commission which they are to receive. On the other hand, stock dealers or jobbers are those who deal in stocks or shares. They are persons who purchase or sell stocks, bonds or other securities on their own account. The distinction between a stockbroker and a stock dealer is clear and well defined.***" (Emphasis supplied) Source: http://digitalcommons.law.yale.edu/cgi/viewcontent.cgi?article=3636&context=ylj. It is noteworthy that William O. Douglas joined the U.S. Securities and Exchange Commission (SEC) in 1934 and in 1937 William O. Douglass became the SEC Chairman. In 1939, when Justice Louis D. Brandeis retired from the Court, President Franklin D. Roosevelt nominated Douglas as his replacement on March 20, and Douglas was sworn in as U.S. Supreme Court Justice on April 17, 1939. Related to the point made by Justice Douglas about the nature of being a stockbroker, it is worthy of note that on 15 March 2018, the United States Court of Appeals for the Fifth Circuit recently held, when it overruled the Department of Labor's creation and expansion of the "best interest" rule to stockbrokers, that stockbroker are "salespeople", not fiduciaries. *See* Chamber of Commerce et al vs. United States Department of Labor et al, Dkt. No. 17-10238, at 8 (5th Cir. 2018). http://www.ca5.uscourts.gov/opinions/pub/17/17-10238-CV0.pdf. *See also* Restatement (Third) of Agency § 8.01 cmt. b (2006): as agent, the stockbroker owes the duty of loyalty ("An agent's failure to provide material information to the principal may facilitate the agent's breach of the agent's duties of loyalty to the principal"), which is distinguishable in the law from fiduciary duty, although many courts use the word "fiduciary" loosely. *See* Justice Douglas' Stock "Brokers" as Agents and Dealers, *supra* at 46: "The blurred fashion in which courts have at times treated the distinctions between stock "brokers" acting on the one hand as agents or on the other as dealers has resulted in several paradoxical situations." In point of law, a stockbroker's duty is grounded in The Law of Agency in conjunction with the Law of Commerce, and therefore covered by the duty of loyalty standard, but this duty ends at the close of the transaction and is not ongoing. Hence the Fifth Circuit's decision is correct. The stockbroker is more like a salesperson than a fiduciary. True the stockbroker – the true traditional Wall Street stockbroker – gives investment advice, but that advice is incidental to the transaction, i.e., the recommendation to the customer to buy or sell or hold a particular security. Compensation paid to the stockbroker – commissions – is baked into the stockbroker's brokerage services, which includes both executing a transaction and giving investment advice to the customer. Historically, this was the definition of a "stockbroker" and this definition should be retained in the SEC proposed "Regulation Best Interest" rule for the *traditional Wall Street style stockbroker* The historical stockbroker is subject to the Law of Commerce (the standard of care being "commercial honor", which, by the way, is already part and parcel of FINRA Rule 2010) and the Law of Agency (the standard of care being the duty of loyalty); but this kind of stockbroker was not subject to the fiduciary standard, which is the "best interest of the client". This makes sense because, in the Law of Commerce, stockbrokers have



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stocks and bonds, and not variable annuities and variable life insurance policies and other investment company securities. But starting in the 1990s "the globalization of the world economy has increased interest in internationally recognized finance designations"[6] that began to be used in order for Firms to "identify qualified practitioners"[7]; in time, these designations became "routinely used in hiring and promotion decisions"[8] at these financial services firms. And so, in the 1990s and early 2000s, insurance agents now wanted to be able to hold themselves out to the public as "professionals", like lawyers and accountants,[9] and not just salesmen; likewise, stockbrokers who did not want to remain simply "traditional Wall Street style stockbrokers" but instead wanted to hold themselves out to the public as "professionals" on the order of lawyers and accountants were encouraged by their Firms, especially the big wire houses, to obtain designations that would enable stockbrokers to hold themselves out to the public as "advisors" (as distinct from "adviser", which is the Investment Adviser Act of 1940 term of art referring to "investment adviser representatives" and "registered investment advisers" properly registered under the Act). As a result financial services professional designations sky rocketed. By the early 2000s, insurance agents became "financial planners", which prompted many States,

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"customers" not "clients"; only fiduciaries, like lawyers and now other professionals like "financial advisors", have "clients" in the same sense that investment advisers under the Investment Adviser Act of 1940 have "clients". This distinction is and remains meaningful in the law and therefore should be maintained in the SEC's proposed "Regulation Best Interest" rule as pertains to "traditional Wall Street style stockbrokers". Adhering to this principle, stockbrokers will still be held to all the duties of commercial honor and duty of loyalty that carries over from the Law of Agency and the Law of Commerce: Namely, the stockbroker's duty of loyalty includes the duty to executing the customer's order in a timely fashion; the duty to complete the transaction in a manner best suited to serve the client's interests; the duty to execute orders only after receiving proper authorization from the customer; and the duty to not engage in market manipulation practices, such as but not limited to front-running and painting-the-tape, bear running, etc. (*See* footnote 31 *infra*) as well as the duty of not violating the prohibition against making an untrue statement of a material fact and omitting to state a material fact that, in its absence, would make the stockbroker's statement misleading to the customer. SEC Rule 10-b(5). For his brokerage services, which includes giving investment advice – even sophisticated investment advice that may span analysis of company "fundamentals" and "technicals" of trading charts – that is incidental to the transaction, the traditional Wall Street style stockbrokers should continue to be subject to the suitability duties already amply covered by FINRA rules, but this duty of suitability should cease at the completion of the transaction and not span the entire series of transactions in the retail customer's portfolio, whether in their entirety or in part, so long as the "traditional Wall Street style stockbroker" does not hold himself out to the public as a "financial advisor" or such other professionally styled title.

[6] Global Alphabet Soup: Internationally Recognized Professional Designations in Finance, Journal of Financial Education, 38 (3/4), Fall/Winter 2012.

[7] Jason Zweig and Mary Pilon, Is Your Adviser Pumping Up His Credentials?, The Wall Street Journal, 16 October 2016, https://www.wsj.com/articles/SB10001424052748703927504575540582361440848

[8] Global Alphabet Soup: Internationally Recognized Professional Designations in Finance, Journal of Financial Education, 38 (3/4), Fall/Winter 2012.

[9] An Accountant is considered, by the Courts, to be fiduciaries to his clients in areas such as tax services and asset management when the accountant positions himself as an expert, and the client places trust in the accountant, and the client is heavily dependent on this advice. *See e.g.*, Iacurci v. Sax, 313 Conn. 786 (Conn.Supr.Ct.2014); Christensen, et al v. Cox, et al., Dkt. 2:17-cv-00222 (U.S.D.C. Utah - 2017); Triton Const. Co. v. Eastern Shore Elec. Servs., Inc., 2009 WL 1387115; Christensen, et al v. Cox, et al., Dkt. 17-01635-BLS1, (Mass. Super.Ct. Suffolk – 2018), Lawyers Weekly No. 09-043-17. Beyond these parameters, CPA accountants are technically not normally considered fiduciaries. That said, the AICPA Professional Code of Conduct highlights the attributes of objectivity, integrity, free of conflicts of interest, and truthfulness. This comes pretty close to the fiduciary standard; and, because of this, a CPA accountant is generally thought to be, in the public's minds' eye, to be a fiduciary. In fact, many CPA Accountants also hold the Certified Financial Planner™ designation, which requires designation holders to operate under a fiduciary standard. As a result, for all intents and purposes, CPA Accountants are deemed to be "professionals" alongside with lawyers, regardless of what the courts may say on this fiduciary subject. And this is the big picture being made in the paragraph to which this footnote is appended: The desire to be and holding oneself out to the public as being a "professional" has consequences.



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and even the SEC, to require insurance agents to register as "investment advisers"[10] (i.e., investment adviser representatives of State or federal registered investment advisers) when they wanted to call themselves "financial planners"; and the same insurance agents who wanted to sell variable annuities, variable life insurance, and mutual funds were required to register as "registered representatives of broker/dealers" – making them, in effect, "stock brokers" – but not real stock brokers in the traditional Wall Street meaning of the word. In the mid-2000s, the SEC accommodated Merrill Lynch so that its stockbrokers would be allowed to hold themselves out to the public as "advisors"[11] (so long as certain somewhat ambiguous conditions were met.) Now practically every practitioner in the financial services industry holds himself out to the public as a "financial advisor", and the outcome is overwhelming confusion in the minds of the investing public, most pronounced in the community of senior citizens. Hence, with so many "financial advisors" marketing themselves as experts under color of so many designations that are confusing to the public[12] and selling and replacing all kinds of investment company securities that have grown exponentially with increasingly complex riders and other "bells and whistle" features, it is easy to reach the conclusion that the time has come for a "Regulation Best Interest" standard. Indeed, the "Regulation Best Interest" proposed rule is nothing more than the logical conclusion to the insurance agent's and stockbroker's aspiration to be recognized as a "professional" and not just a "salesman".

What does not make sense is the application of the proposed "Regulation Best Interest" rule to ***stockbrokers who are proud of who they are – traditional Wall Street stockbrokers engaged exclusively or nearly exclusively in transactional securities business for investors who want to Actively Trade*** – that is, engage in ***in-and-out trading of equities*** and/or their derivatives in brokerage accounts.

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[10] *See* When Does a Financial Planner Become an Investment Adviser? Society of Financial Service Professionals, Financial Planning Section News and Views, 3rd Qtr, 1999-2000, Vol. 2, No. 3, where this author cautioned, "Don't allow yourself to fall victim to a perceived 'identity crisis'. If you are insurance agent and are good at being an insurance agent, but your heart is really not into complying with regulations requisite for being an investment adviser, then take pride in what you do. Go back to calling yourself an insurance agent. Don't hold yourself out to the public as a "financial planner". * * * Therefore, if you are an insurance agent, attorney, CPA, ChFC, CFP, or other financial services professional who has a strong desire to wear the title "financial planner" for personal or market reasons; and, if the equities market is where you want to be, then you should prepare yourself for registering as an "investment adviser" with either your State Securities Regulator or with the U.S. Securities and Exchange Commission." Id. at 6.

[11] *See* SEC's "Merrill Lynch Rule" Struck Down by the US Court of Appeals: "The SEC rule allowed stockbrokers to act as "advisors" and to charge percent of assets fees. Prior to this rule, only investment advisors who registered with the SEC or with the states and who were regulated under the Investment Advisers Act of 1940 were permitted to do this. Under the Merrill Lynch Rule, brokers could call themselves advisers, yet remain exempt from regulation under the Investment Advisers Act, as amended." http://www.theskilledinvestor.com/ss.item.232/secs-merrill-lynch-rule-struck-down-by-the-us-court-of-appeals.html. Merrill Lynch and the wire houses believed that, calling their brokers "advisors" (with an "OR") as opposed to "advisers" (with an "ER") would be sufficient to distinguish a stockbroker (who gives advice that may not-be-so-incidental to their brokerage business) would be sufficient to distinguish their brokers from bona fide registered investment advisers and investment adviser representatives. This worked for a while, even after the D.C. Circuit reversed the Merrill Lynch Rule in Financial Planning Association, Inc. v. SEC, 482 F.3d 481 (D.C. Cir. Mar. 30, 2007). But the technical, legal distinction between "advisor" and "adviser" is not so easy for the investing public to understand, especially with respect to the importance this distinction might have in regards to fiduciary duty that the financial services processional does or does not owe to the investing customer or client. Accordingly, in Release No. 34-83062; the SEC proposes to "restrict broker-dealers and associated natural persons of broker-dealers, when communicating with a retail investor, from using as part of a name or title the term "adviser" or "advisor" in certain circumstances." *See* SEC Commissioner Kara M. Klein, Statement on Proposals Relating to Regulation Best Interest, Form CRS, Restrictions on the Use of Certain Names or Titles, and Commission Interpretation Regarding the Standard of Conduct for Investment Adviser, https://www.sec.gov/news/public-statement/stein-statement-open-meeting-041818 (April 18, 2018).

[12] *See* Consumer Protection Bureau, Senior Designations for Financial Advisers: Reducing Consumer Confusion and Risks, (April 18, 2013): "The titles and acronyms for the different designations are often similar or nearly identical to other designations, making it difficult for consumers to distinguish between different designations' qualifications or legitimacy." Id. at pp. 6-7.

## 2. The Inequity of the "Regulation Best Interest" Rule for Active Trading and Why an Exception to the Rule, as Proposed, Should be Created.

It would be worthwhile to recite stock market behavior in the history of the Stock Market in mid-1970s and the 1980s before the so-called "democratization of the stock market" in the 1990s before we discuss why the "Regulation Best Interest" proposed rule would be *inequitable* to *both* customer and stockbroker in the Active Trading forum.

As interest rates offered by banks fell, U.S. Households moved financial assets from bank deposits to equity ownership in mutual funds, jumping from 22 percent in 1975 to 42 percent in 1999.[13] The reason for the movement of assets from banks to the stock market from the 1980s to end of the 1990s has been explained as follows:

- The CD market reached its historical high on July 3rd 1984 when the 5 year CD reached a high of 12.06% and the 1 year CD reached a high of 11.27% and the 6 month CD reached a high of 10.91%.[14]

- The CD market at the beginning of 2000 had fallen, on July 5th 2000, to 6.16% for 5 year CDs, to 5.63% for 1 year CDs, and to 5.25% for 6 month CDs.[15]

In contrast, the Dow Jones Industrial Average, the S&P 500, and the Nasdaq Composite indices *each gained more than 900 percent* between 1980 and 1998.[16]

Hence, equity ownership in the United States grew dramatically in the 1980s and the 1990s: Total holdings of equities by U.S. Households rose from 17.2 percent of household financial assets in 1980 to 34.9 percent in 1998.[17]

The Federal Reserve Bank of New York has broken down these total holdings of equities over these twenty (20) years as follows:

- In 1989, the average asset allocation among U.S. Households was **5.0% in Stocks** and 24.6% in retirement and other managed accounts that did not include investments directly in stocks and bonds.[18]

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[13] John V. Duca, The Democratization of America's Capital Markets, Federal Reserve Bank of Dallas, Economic and Financial Review, Second Quarter 2001, at 13 ("The Democratization of Household Investors' Access to Capital Markets"). Source: https://www.dallasfed.org/~/media/documents/research/efr/2001/efr0102b.pdf.

[14] Bankrate, Historical CD Interest Rates – 1984-2016, https://www.bankrate.com/banking/cds/historical-cd-interest-rates-1984-2016/

[15] Id.

[16] *See* Equity Ownership in America, Investment Company Institute and the Securities Industry Association, Fall 1999, at 1. Source: https://www.ici.org/pdf/rpt_equity_owners.pdf.

[17] *See* Equity Ownership in America, Investment Company Institute and the Securities Industry Association, Fall 1999, at 1.

[18] *See* Federal Reserve Bank of New York, Stocks in the Household Portfolio: A Look Back at the 1990s, Current Issues in Economics and Finance, Volume 7, No. 4 (April 2001), at 2. Source: https://www.newyorkfed.org/medialibrary/media/research/current_issues/ci7-4.pdf.



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- In 1998, the average asset allocation among U.S. Households jumped to **11.6% in Stocks**, with a corresponding decline to 21.7% in retirement and other managed accounts that did not include investments directly in stocks and bonds.[19]

As evidenced by these statistics, it is understandable why retail investors flooded into the stock market in the mid-1980s and well into the 1990s, until the end of the dot.com bubble in 1999.

But, with the onset of the Great Recession that started in 2008-2009, ***direct*** [20] stock ownership by middle-class began to retreat.[21]

And today, ***middle-class direct stock ownership has declined as dramatically*** as it rose in the 1990s.[22]

Today, the lion's share ***direct stock ownership has returned to the wealthier households***. This is confirmed in a very recent 2018 article written by a Certified Chartered Analyst, where the author writes:

> "According to research from the New York University economist Edward Wolff, the top 10 percent of American households now own 84 percent of all stocks. That's up from 77 percent ownership in 2001. * * * Just 27 percent of the middle class owns at least $10,000 in equities, compared with 94 percent of the wealthiest households."[23]

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[19] Id. at 2.

[20] As opposed to "indirect" stock ownership via owning an interest in or share of a portfolio of stocks, such as in a retirement fund, or in the separate account of a variable life or variable annuity product, or a mutual fund. Hence, by "direct", I mean owning the individual stock, whether in journal entry or stock certificate form, outside of a portfolio of securities collectively owned by others, whether the company is blue chip or NASDAQ, and even OTCBB Pink stock.

[21] *See* Justin McCarthy, Just Over Half of Americans Own Stocks, Matching Record Low, (Gallup, 20 April 2016): "In 2007, nearly two in three American adults (65%) reported investing in the stock market, the high in Gallup's selected trend on this question for April of each year. But this percentage shrank each year from 2008 to 2013 * * * While a slight majority of Americans report investing their money in the stock market, it's a far cry from the pre-recession levels that spanned 58% to 65%." Source: https://news.gallup.com/poll/190883/half-americans-own-stocks-matching-record-low.aspx.

[22] *See* Jeffrey M. Jones, U.S. Stock Ownership Down Among All but Older, Higher Income, (Gallup, 24 May 2017): "U.S. stock ownership rates are highly related to income, ranging from 21% among those with an annual household income of less than $30,000 to 89% among those with an income of $100,000 or more. * * * As a generation, baby boomers – all of whom were in their prime working years during the economic boom of the 1980s and 1990s, and many of whom likely had 401(k)s at work – have above-average rates of stock ownership. * * * The stock market has performed well in 2017, but proportionately fewer Americans are benefiting from today's bull market than did so in bull markets before the financial crisis [i.e., the 2008 Great Recession]. The gains in stock values in recent years seem to have done little to persuade people who may have divested themselves of stocks to get back in the market. Nor has the recovery encouraged new investors to join the market. Although young adults are understandably less likely than their elders to own stocks, the percentage of 18- to 29-year olds investing is down 11 points since before the financial crisis." (Emphasis supplied) Source: https://news.gallup.com/poll/211052/stock-ownership-down-among-older-higher-income.aspx.

[23] Benjamin P. Carlson, CFA, Inequality in the Stock Market, http://awealthofcommonsense.com/2018/02/inequality-in-the-stock-market/ (Emphasis supplied) citing Edward N. Wolff, Household Wealth Trends in the United States, 1962 to 2016: Has Middle Class Wealth Recovered?, NBER Working Paper No. 24085, Issued in November 2017. Mr. Carlson's CFA credentials are confirmed: CFA charter was awarded on 2 September 2010. Mr. Carlson's CFA designation is active. Mr. Carlson is Director of Institutional Asset Management at Ritholtz Wealth Management (AUM 250 million < 1 billion) Grand Rapids, Michigan. Credential Confirmation at https://www.cfainstitute.org/community/membership/directory/pages/results.aspx?uid=475319.



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Based on the evidence that the stock market, today, has returned to the "stock ownership being concentrated at the top", the argument advanced here – that the Active Trader and his stockbroker should be exempted from the application of the proposed "Regulation Best Interest" rule – can reduced to this Carve-out Exemption Formula:

When the equity or its derivative investor is one who:

- Is among "the top 10 percent … who own 84 percent of all stocks";
- Is among "the 94 percent of the wealthiest households" who own "at least $10,000 in equities";
- Is independently wealthy;
- Has set aside a portion of their wealth earmarked for Active Trading;
- Is an investor for whom concepts like "turnover rate" and "cost-to-equity" have ***no material bearing on or meaning for*** his stock market investment conduct;
- Is among a niche breed of investors for whom "in-and-out trading" is simply "***a given***"; and,
- Is an investor for whom "investor losses due to market or other risks inherent in investing" is likewise simply "***a given***",

the Active Trader and his traditional Wall Street stockbroker should be exempted from the application of the proposed "Regulation Best Interest" rule because, to not do so, would be *inequitable* to *both* customer and stockbroker in the Active Trading forum. The following jurisprudence supports this conclusion premised on the aforementioned statistics supporting the case that ***direct stock ownership has returned to the wealthier households***:

"Law without principle is not law; law without justice is of limited value. Since adherence to principles of 'law' does not invariably produce justice, equity is necessary." Simonds v. Simonds, 45 N.Y. 2d 233 (1978). Hence, the reason and necessity for Equity: As U.S. Supreme Court Justice Joseph Story has written, "Thus, Aristotle has defined the very nature of equity to be the correction of law, wherein it is defective by reason of its universality." Story, 1 Commentaries on Equity Jurisprudence 3, The Lawbook Exchange (2006). Equitable principles are "unquestionably principles of right, justice and morality[.]" Id. The U.S. Supreme Court has stated: "Equity eschews mechanical rules; it depends on flexibility." Holmberg v. Ambrecht, 327 U.S. 392, 396 (1946). Justice Oliver Wendell Holmes, Jr., wrote: "The life of the law has not been logic: it has been experience….and it cannot be dealt with as if it contained only the axioms and corollaries of a book of mathematics." The Common Law at 1 (1881).

***Anecdotally***, the truth of our proposed Carve-out Exemption Formula and the relevance of the aforementioned propositions of law and equity can be amply demonstrated through my first-hand experience involving a relative of mine who was an Active Trader.

My relative was the son of an immigrant. My relative's father started a small construction business before the Great Depression and, after the Depression, did better than survive. My relative never graduated high school. My relative worked for his father as a stone mason – in those days, houses were built with stone and brick, not



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toothpicks. When America entered the Second World War, my relative joined the Navy as a Seabee[24] - a construction worker who, while being shot at by the enemy, built pontoon bridges and make-shift runways and fixed damaged ships essential for his Army, Navy, and Marine colleagues to carry on the offensive against the enemy. When my relative returned home from the War, he eventually branched out on his own from his father's business and built his own construction business. My relative was an *entrepreneur par excellence*. Because of the nature of his construction business, he also invested in real estate. He made money and he lost money both in his business and his real estate investments. But by the time he approached retirement years – *and this is relevant to his source of funds and wealth profile* – he had made millions; however, at the insistence of his wife, the lion's share of his savings was kept in bank deposit savings controlled by his wife. My relative agreed to let this money be off-limits to himself because – *and this relevant to his investor KYC or "know your customer" profile* – he was a gambler, literally. If you went to his home, in his TV room you'd find a large black chalk board. On this chalk board was scribbled the name of every local race track, each race horse (and its win/loss statistics, along with age, weight, estimated speed), each jockey (again, win/loss statistics, along with age, weight, and experience of the jockey), and each race track's positives and negatives and maintenance record. My relative was also a card player. Friday nights were smoke-filled poker nights at my relative's house, and the card games lasted into early Saturday morning hours. But he was no amateur. He was a bona fide card reader. Only "professional" players were invited to play on Friday card nights at his house – indeed, one of these "professionals", a well-known ballplayer on a one of the 1970s Super Bowl teams, was a "regular" during off-season. In short, my relative was a risk-taker through and through – *again, this is relevant to his investor risk profile*: My relative was a risk-taker whose willingness to take risks was off-the-charts. Today, on a new account form we would check the box for "speculative" investor who wants to engage in "speculation" in the stock market; but even these boxes would not accurately reflect who he was when it came to being an investor in the stock market: He was an Active Trader. Because of his gambler/entrepreneurial spirit, my relative's wealth was, as we said, divided: The lion's share for the family, and "play money" for my relative. My relative's wife "allowed" him to keep a small amount (approximately $500k to $1mm) – *and this is relevant to the investor financial objective profile* – as "entertainment money". My relative opened a brokerage account with a traditional brokerage firm and hired a broker to help him trade actively, i.e., engage in "in-and-out trading", which he did regularly throughout the 1980s, 1990s, and early 2000s. My relative liked to boast that he "he lost 20 or 30 thousand *today* in the market" *because – and this is relevant to his investment objective profile* – the second part of his boast was, "But I'll make it up *tomorrow*" and "I'll double my money *tomorrow*". Sometimes he made good on his boast; sometimes he didn't. It didn't matter to him. Active Trading was his "entertainment" and a "legitimate" substitute for gambling – *again, relevant to the investor financial objective profile*. As a bona fide "in-and-out" Active Trader, concepts like "turnover rate" and "cost-to-equity" and "commission-to-equity" ratios would have been *meaningless* for my relative: High aggregate commissions paid to his broker were a *fair quid-pro-quo* for the oodles of time that his broker allotted to my relative for "talking shop". My relative understood that his broker's *knowledge of the stock market* was literally his *broker's stock-in-trade*. This broker was your traditional Wall Street stockbroker. And paying for this knowledge was only fair. How much to pay was always negotiable. This give-and-take is part of the overall experience of the market place and the essence of being an Active Trader. Both broker and the active trading customer are focused on their own self-interest. That is a given. Protecting my relative, for his own good, from his broker's self-interest would have made no sense to my relative. So long as the customer is getting what he is paying for, there is no need for government protection. This is the nature of contracts. My relative understood that his

[24] That is, the United States Naval Construction Battalions, better known as the Seabees. The Seabees consisted of skilled workers who were trained to drop their tools if necessary and take up their weapons at a moment's notice to defend themselves. The concept model was that of a USMC–trained battalion of construction tradesmen (a military equivalent of those civilian companies) that would be capable of any type of construction, anywhere needed, under any conditions or circumstance.
Source: https://en.wikipedia.org/wiki/Seabee.



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broker was sharing his knowledge, and commissions charged by the broker were a fair price in exchange for the knowledge that my relative wanted. My relative, who had no high school diploma or college degree, acquired a wealth of knowledge from his broker – he learned how to analyze "fundamentals" of companies and how to presage "technicals" of trading charts in order to both understand *and challenge* his broker's stock picks when they "talked shop". This knowledge for a man with no formal education was a source of immense pride for my relative. If a regulator were, in those days, to insist that my relative needed protection against his broker – so-called high risk brokers – in order to protect my relative against "investor losses due to market or other risks inherent in investing" that result from "in-and-out trading", this good-intention-paternalism would have been unintelligible to my relative. My relative would have responded: It is 'not the business of government' to tell him how he can or should spend his money and whom he can hire to do his "in-and-out trading".

We fully appreciate the fact that this evidence is anecdotal. But that does not take away from the important fact that there is a small population of investors who, because of their life's experiences, are extreme risk-takers, who "play the market" (and want to continue to have brokers who will enable them to "play the market"), and most importantly, legally speaking, that these Active Traders have as much a right to engage in ***in-and-out*** trading in the market – "gamble", in other words, in the market – just as the rest of the population has a right to "invest" (whether "invest" means "investing conservatively", "investing aggressively", or "investing speculatively" in the market). In other words, there is de facto a unique category of investor who does not fit the profile of investors that, to date, regulators have identified for suitability and investor profile purposes. Especially for this reason, the "Regulation Best Interest" standard does not, and should not, apply to these investors that we have called and referred to as "Active Traders" in this Comment Letter.

To sum up, if my relative were alive today, he would have been one of those "top 10 percent of American households owning 84 percent of all stocks" and among that "94 percent of the wealthiest households" who hold "at least $10,000 in equities" and trade stocks regularly. He was an Active Trader in his day, and would have been an Active Trader today. If the trade-off for protecting my relative against "turnover ratios" and "cost-to-equity" and "commission-to-equity" ratios meant that my relative would be unable to find a ***traditional Wall Street stockbroker*** to do my relative's "in-and-out trading" – *this government protection against his broker's self interest* would <u>not</u> be in my relative's best interest. Limiting my relative's universe to brokers whose skill-set is limited to investment company securities, even if they be subject to the "Regulation Best Interest" standard, would <u>not</u> be in my relative's best interest. Accordingly, precisely because (as has been shown) the stock market has, since 2008, retreated dramatically from the "democratization" of the 1990s, the SEC should take this factor into consideration, in 2018, <u>for the benefit of those investors who are independently wealthy and who have set aside a portion of their wealth earmarked for Active Trading</u>. This is the equitable thing to do: The universality of the proposed "Regulation Best Interest" rule brings about justice for the 90% of the American Households who need the brakes put on brokers with designations who need the brakes put on them; but, the universality of the "Regulation Best Interest" rule as proposed is inequitable – denies justice – for those "top 10 percent of American households owning 84 percent of all stocks" and for that "94 percent of the wealthiest households" who hold "at least $10,000 in equities" and engage in "in-and-out trading" – for Active Traders, in other words, like my relative. For this reason, the "Regulation Best Interest" rule, as proposed, needs correction.[25]

[25] It bears repeating here: "Law without principle is not law; law without justice is of limited value. Since adherence to principles of 'law' does not invariably produce justice, equity is necessary." <u>Simonds v. Simonds</u>, 45 N.Y. 2d 233 (1978). Hence, the reason and necessity for Equity: As Justice Joseph Story has written, "Thus, Aristotle has defined <u>the very nature of equity to be the correction of law</u>, wherein it is <u>defective by reason of its universality</u>." Story, 1 <u>Commentaries on Equity Jurisprudence</u> 3, The Lawbook Exchange (2006). Equitable principles are "unquestionably principles of right, justice and morality[.]" <u>Id</u>. The U.S. Supreme Court has stated: "Equity eschews mechanical rules; it depends on flexibility." <u>Holmberg v. Ambrecht</u>, 327 U.S. 392, 396 (1946). Justice Oliver Wendell



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3. **How the Inequity or Deficiency of the "Regulation Best Interest" Rule, as Proposed, Should be Remedied for the Traditional Wall Street Stock Broker Engaged in Active Trading for Suitable Customers.**

Accordingly, we propose that there should be an exception carved out from the "Regulation Best Interest" proposed rule to accommodate this class of investors and their brokers who specialize in Active Trading. We propose that the Carve-Out Exemption Formula be focused on the following factors:

- The Active Trader demonstrates that he or she has a long track record of having an entrepreneurial spirit and experience as an "off-the-chart" risk-taker or has otherwise demonstrated his understanding of the risks of active trading.

- The Active Trader demonstrates that he or she fits into the "the top 10 percent … who own 84 percent of all stocks" category.

- The Active Trader demonstrates that he or she fits into the "the 94 percent of the wealthiest households" who own "at least $10,000 in equities" category – direct, not indirect, equities.[26]

- The Active Trader demonstrates that he or she is wealthy, the majority of his or her wealth having come from entrepreneurial enterprise or inherited wealth or investment proceeds as well as corporate stock options, and other corporate remuneration that places the investor in the 10% category above.

- The Active Trader demonstrates that he or she has set aside a portion of their wealth earmarked for Active Trading.

- The Active Trader demonstrates that he or she be willing to evidence the size of his or her wealth; demonstrate that his or her "play money" is legally separated from the lion's share of his wealth that has been legally isolated and protected against the Active Trader's stock market conduct; and be willing to supply other details demonstrating that "investor losses due to market or other risks inherent in investing" will not negatively impact the livelihood of his or her family and business or have a material effect on their lifestyle.

- The Active Trader acknowledges in an informed consent writing that "turnover rate" and "cost-to-equity" and "commission-to-equity" rations have *no material bearing on or meaning for* his past, present, and future stock market investment conduct.

- The Active Trader's broker demonstrates that he or she has entered into a written Active Trading agreement with stockbroker having an established track record of demonstrating that he or she is a traditional Wall

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Holmes, Jr., wrote: "The life of the law has not been logic: it has been experience….and it cannot be dealt with as if it contained only the axioms and corollaries of a book of mathematics." The Common Law at 1(1881).

[26] It bears repeating here: By "direct", I mean owning the individual stock, whether in journal entry or stock certificate form, outside of a portfolio of securities collectively owned by others, whether the company is blue chip or NASDAQ and even OTCBB Pink stock. "Indirect" refers to stock ownership via owning an interest in or share of a portfolio or collection of stocks, such as in a retirement fund, or in the separate account of a variable life or variable annuity product, or a mutual fund. According to UPFINA, as of January 11th 2018, 50% of households own no stock; 13.9% of households directly own stock; 35.4% of households only indirectly own stock (e.g., via 401k accounts). Source: https://upfina.com/50-of-households-own-no-stocks/.



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Street stockbroker (as opposed to an investment company securities broker who has dabbled in picking stocks).

As Alexander Hamilton points out in the Debates in the Federal Convention of 1787: "In every community where industry is encouraged, there will be a division of it into the ***few*** and the ***many***. Hence, separate interests will arise. * * * Give all power to the many, they will oppress the few. Give all power to the few, they will oppress the many. Both, therefore, ought to have power, that each may defend itself against the other."[27]

This, then, is the purpose of government, according to America's First Secretary of the Treasury, Alexander Hamilton: To indeed protect the interests of the many, *but equally so to protect the interests of the few*.

As the "Regulation Best Interest" proposed rule currently stands, the SEC has set forth measures that will protect the interests of the ***many***; but, in the course of applying the same standard that protects the many, this proposed rule, wittingly or unwittingly, is prejudiced against the ***few***.

For this reason, it is respectfully requested that the SEC seriously consider the factors[28] set forth above in the proposed Carve-Out Exemption Formula (and we welcome the SEC and Industry Members to propose additional factors) in order to *protect the interests of the few* – 10% or so[29] who are Active Traders[30] who are

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[27] A. Hamilton, Esq., 18 June 1787. (Yale Law School Goldman Law Library) http://avalon.law.yale.edu/18th_century/debates_618.asp.

[28] We respectfully request that the SEC take additional factors into consideration when mulling over the importance that this Carve-Out has for the marketplace. First, the Active Trader provides liquidity to the market generally, but also specifically for individual stocks. Second, Active Traders benefit "buy and hold" investors: Active Traders provide for the more conservative investor a "ready, able, and willing" contra-party for a transaction, either the liquidation or purchase of a security at the best price ***precisely when*** the "buy and hold" investor wants to trade. Third, certain individuals trace their wealth to their ability to trade the market. These comprise a segment of the "few" whose interests Alexander Hamilton says that government in a republican form of government is required to protect when the government is focused on protecting the interests of the "many". The form of government that the Founders of our Country and the Framers of our Constitution have given us was deliberately crafted to enable all individuals the opportunity to lift themselves up from their current economic status, whatever that might be for each given individual. The stock market affords one of these essential economic opportunities for accomplishing this. The "Regulation Best Interest" rule, as currently proposed, if imposed in broad-brush fashion so as to impose the fiduciary standard on a certain special kind of stockbroker – the Traditional Wall Street Stockbroker – will invariably drive out of the marketplace the very kind of stockbroker who, from the beginning of the Stock Exchange in Philadelphia founded in 1790 and the New York Stock Exchange founded in 1792, made the American stock market the envy of the free world.

[29] *See* Heidi Shierholz, The 'democratization of the stock market' that never happened, Economic Policy Institute (26 September 2012): "Despite minute-by-minute dissection of the stock market in the news media, the share of the population owning stock is surprisingly low, even when including share purchased indirectly through retirement accounts. In 2010, less than half (46.9 percent) of all households had stock holdings, and less than a third (31.1 percent) had stock holdings of $10,000 or more. The imbalanced distribution of stock assets persisted over time, as seen in the figures below from the newly releases ***State of Working America, 12th Edition*** [figures not included here, but accessible in the link provided]. The wealthiest 1 percent of households has never held less than one-third of all stock wealth. Since 1989, the top fifth of households consistently held about 90% of stock wealth, leaving approximately 10 percent for the bottom four-fifths of households. * * * " (Emphasis supplied) Source: https://www.epi.org/publication/wealth-stock-market-holdings/.

[30] We acknowledge that the SEC already has a carve-out for the "Day Trader". We are requesting that the SEC create a carve-out for the "Active Trader" as distinguished from the "Day Trader". Generally speaking, Active Trading is a high-volume short-term investment strategy that aims at eking out a profit from the daily price fluctuation of target stocks; but trading occurs, maybe, only once or twice a week within a short period of time (e.g., a month); exception reports for most clearing firms have set an Active Trading threshold at ten (10) trades per month. Day Trading, on the other hand, occurs when a customer executes four or more stock or options day-trades within a much shorter period of time (usually a four- or five-day period) in a margin account. On a different but related note, we point out that the SEC does not appear to have addressed whether an Active Trading account with an online broker/dealer would be treated differently from an Active Trading account with a broker/dealer that does not operate via an online trading model.



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interested in trading individual stocks (as opposed to invest in a portfolio or fund of stocks) with a great degree of regularity, as well as protect the interests of the Active Trader's stockbroker who has an established track record of being a traditional Wall Street stockbroker in order to service the Active Trader.

## 4. Conclusion

We believe that the "Regulation Best Interest" rule, as proposed by the SEC, is the logical outcome of insurance agents and stockbrokers wanting to rise from the status of "salesman" to that of "professional"; obtaining the many financial services professional designations available to them in the current "certification and designation" marketplace has now entrenched them as "financial services professionals".

"Professionals" are held to a fiduciary standard, pure and simple; "salesmen" are not and should not be.[31]

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[31] The "Regulation Best Interest" rule, as proposed by the SEC, would broad-brush fiduciary duties on Stockbrokers who are strictly transactional brokers as opposed to stockbrokers who are "financial advisors", despite the fact that the federal courts have consistently maintained that stockbrokers are essentially salesmen and therefore have, in only very narrow and specific aspects of their services, imposed fiduciary-like duties on Stockbrokers who are strictly transactional. . For stockbrokers acting in a non-discretionary capacity, the federal courts operate under the following principle: "the scope of any duties owed by the broker will generally be confined to executing the investor's order." Martinez Tapia v. Chase Manhattan Bank, N.A., 149 F.3d 404, 412 (5th Cir. 1998). When executing client orders in non-discretionary accounts, brokers are charged with the duties of "diligence and competence" – which is not a fiduciary standard. De Kwiatkowski v. Bear, Stearns & Co., 306 F.3d 1293,1302 (2d Cir. 2002). Stockbrokers executing customer orders in non-discretionary accounts must complete transactions "in a manner best suited to serve the [client's] interests" and "brokers may execute orders only after receiving proper authorization from the customer"– again, not a fiduciary standard. Leib v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 461 F. Supp. 951, 953 (E.D. Mich. 1978), *aff'd*, 647 F.2d 165 (6th Cir. 1981). Once the broker diligently and *competently consummates* the transaction on the client's behalf, most federal courts have held that "the broker's *responsibility to his customer ceases.*" Id. Furthermore, the broker "*has no continuing duty*" to the customer with respect to that transaction once the transaction is consummated. Id. Finally, the broker is not required to "keep abreast of financial information which may affect his customer's portfolio or to inform his customer of developments which could influence his investments. Id. Even where stockbrokers demonstrate a greater level of involvement in their clients' financial decisions by providing recommendations, even sophisticated investment advice, in *non-discretionary* accounts, courts have consistently reiterated that whatever duty a broker owes ends once the transaction has been completed. The stockbroker's advice to the client "triggers no ongoing duty" to the client and the client "has no legal claim on the broker's ongoing attention." De Kwiatkowski v. Bear, Stearns & Co., 306 F.3d 1293, 1302 (2d Cir. 2002) (citing Press v. Chem. Inv. Servs. Corp., 166 F.3d at 536 (finding a broker's fiduciary duty is limited to the "narrow task of consummating the transaction requested") *and see* Independent Order of Foresters v. Donald, Lufkin & Jenrette, Inc., 157 F.3d 933, 940-41 (2d Cir. 1998) (finding that in a non-discretionary account, "the broker's duties are quite limited" including the duty to obtain client's authorization before making trades and to execute requested trades). So long as the stockbroker does not charge a fee for his investment advice, separate from and/or in addition to his transaction commissions, the stockbroker remains a stockbroker and not an investment adviser. These federal principles make perfect sense when the stockbroker is operating in a strictly transactional role with respect to the customer in a non-directionary account.

That said, even when the strictly transactional stockbroker is acting in a non-discretionary capacity, the stockbroker is "obliged to give honest and complete information." De Kwiatkowski v. Bear, Stearns & Co., 306 F.3d 1293, 1302 (2d Cir. 2002). This duty also includes "the duty to refrain from self-dealing or refusing to disclose any personal interest the broker may have" as well as "the duty not to misrepresent any fact material to the transaction." Leib v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 461 F. Supp. 951, 953 (E.D. Mich. 1978), *aff'd*, 647 F.2d 165 (6th Cir. 1981). These duties approach fiduciary; but again, the duty ceases at the close or settlement of the transaction. Similarly, stockbrokers are required to make recommendations only after developing a sufficient understanding of the nature and risks involved with a given transaction. Id. And, stockbrokers must also describe to their client the risks involved and the potential implications of recommended transactions. Id. Again, these duties approach fiduciary; but these duties cease at the close or settlement of the transaction; ultimately, these duties derived from federal court jurisprudence are not fiduciary duties, but rather suitability duties, which are covered in the FINRA market conduct rules.

The logic of these two leading Second Circuit cases - International Order of Foresters v. Donaldson, Lufkin & Jenerette, 157 F.3d 933, 940 (2d Cir. 1998) and De Kwiatkowski v. Bear, Stearns & Co., 306 F.3d 1293 (2d Cir. 2002) - is that, in a non-discretionary account, a broker is presumed to not be held to a fiduciary relationship until *both* of these two critical elements occur: (1) reliance by the customer



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The "Regulation Best Interest" standard is the logical quid quo pro for becoming a credentialed "financial advisor" or credentialed "financial services professional".

The "Regulation Best Interest" standard works justice for the 84% to 90% percent of the American Households serviced by these financial service professionals.

That said, the universality of "Regulation Best Interest" rule, as proposed, works an injustice for remaining 10% or so who are Active Traders interested in trading individual stocks (as opposed to investing in a portfolio or fund of stocks) on a regular basis. This proposed rule likewise works injustice for the Active Trader's traditional Wall Street stockbroker.

Because law is universal in nature and applied equally to everyone, all laws are – and, here, this regulation is – by nature defective. The "Regulation Best Interest" rule, as proposed, needs correction as a matter of equity in order to correct the injustice worked on the few to whom this rule and its application does not make sense. In this Comment Letter we have put forth measures that aim at correcting inequity of the "Regulation Best Interest" rule as proposed.

Respectfully submitted,

**NETWORK 1 FINANCIAL SECURITIES, Inc.**

BY: ______________________
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Michael Molinaro, Chief Compliance Officer

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on the broker, and (2) *domination and control by the broker*. *See also* U.S. v. Chestman, 947 F.2d 551, 568-69 (2d Cir. 1991) (*en banc*). "Dominance and control by the broker" is what transports a stockbroker's duty into the realm of fiduciary.

Historically, when the stockbroker trades in a customer's account on a *discretionary* basis the fiduciary standard is, of course, triggered, according to the federal courts. This Comment Letter does not challenge this, nor does it challenge the SEC's "Regulation Best Interest" fiduciary standard for stockbrokers when the customer account is being traded on a discretionary basis. Rather, this Comment Letter challenges the SEC's "Regulation Best Interest" fiduciary standard *when it is expanded to cover all stockbroker conduct, in effect overruling the federal court decisions* set forth above, as for example, Martinez Tapia v. Chase Manhattan Bank, N.A., 149 F.3d 404, 412 (5th Cir. 1998); De Kwiatkowski v. Bear, Stearns & Co., 306 F.3d 1293, 1302 (2d Cir. 2002); and Leib v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 461 F. Supp. 951, 953 (E.D. Mich. 1978), *aff'd*, 647 F.2d 165 (6th Cir. 1981) – which decisions clearly hold that "the scope of any duties owed by the broker will generally be confined to executing the investor's order", which duties are suitability, not fiduciary, duties. This principle of law should be the foundation for the "Regulation Best Interest" rule, as proposed by the SEC, when treating with traditional Wall Street stockbrokers trading for Active Trading customers in non-discretionary accounts.



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