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S7-19-03

October 7. 2003

RECEIVED
OCT 08 2003
OFFICE OF THE SECRETARY

William H. Donaldson, Chairman
Securities and Exchange Commission
450 Fifth Street, NW
Washington, DC 20549

Dear Mr. Donaldson:

The American Federation of State, County and Municipal Employees, commissioned a survey of the nation's 100 largest public pension plans regarding the need for proxy access for director nominations and under what circumstances such a right be used. The government and public affairs firm of Lussier, Gregor, Vienna & Associates. Inc. of Alexandria, undertook the survey during the month of September. The key findings of the survey of public funds with $1.26 trillion in total assets indicate that:

- 80% of the funds think that it's important (30% extremely important; 37% very important; and 13% important) to empower groups of shareholders, to use a corporation-s proxy to nominate directors as a method to improve corporate governance. These funds represent 1.187 trillion dollars in assets.

- Nearly 70% of the funds that administer their own proxy voting policy can foresee a situation in which their fund, either individually or with a group, would seek to nominate candidates on the company proxy card.

- 78% of the funds would consider voting for a shareholder nominated slate.

- The most significant reasons why a public fund might nominate director candidates are:

  ✓ The incumbent board ignored a majority shareholder vote
  ✓ The corporation has issued significant financial restatements
  ✓ The corporation suffers from long time poor financial performance

- Although the public funds see the ability to nominate director candidates as a very important new rule, they clearly don't see it being abused. 55% of the funds indicated that shareholder candidates would be nominated **in** fewer than 15 instances annually; only seven plans predicted that it would occur more that 25 times per year.

- More than 80% of the funds think that shareholders should have access to the proxy card at the next annual meeting.

The full results reveal a number of important details about public fund proxy voting patterns, such as the reasons why shareholders vote against board nominees, and under what conditions they think proxy access should be utilized.

We have enclosed a copy of the survey results for your consideration.

Sincerely,

Gerald W McEntee

GERALD W. McENTEE
International President

GWMcE: rfh
Enclosure

cc: Paul S. Atkins, Commissioner
Roel C. Campos, Commissioner
Cynthia A. Glassman, Commissioner
Harvey J. Goldschmid, Commissioner
Alan L. Beller, Director, Division of Corporation Finance
Martin Dunn, Deputy Director, Division of Corporation Finance
Jonathan G. Katz, Secretary

Public Pension Funds Strongly Support Broad Proxy Access Rights for Director Elections

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- Timing is important. More than 80% of the funds think that shareholders should have access to the proxy card at the next annual meeting.

* * *

- The three most significant reasons why public funds currently withhold their votes from corporate nominated directors are:

  - ✓ Major financial scandal
  - ✓ Not an independent director/potential conflict of interest
  - ✓ Excessive absenteeism

Survey responders provide primarily defined benefit retirement benefits to state, county and municipal employees, teachers, public safety personnel and other specialized groups. 77% maintain a proxy voting policy that is maintained either internally or through a proxy service.

The survey of the nation's 100 largest public pension plans based on asset value was conducted between September 9 and **30,2003** by the government and public affairs firm of Lussier, Gregor, Vienna & Associates, Inc. of Alexandria, VA.

RECEIVED
OCT 06 2003
OFFICE OF THE SECRETARY

December 18,2002

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

Re: Proposed Rule Change Pursuant to 17 CFR 240.19b-4

Dear Mr. Katz:

Mutual Service Corporation ("MSC") is a fully disclosed retail broker-dealer registered to conduct business in fifty (50) states and with over 1,600 Registered Representatives offering securities services through 926 Branch Offices ("Offices") of which 248 are Offices of Supervisory Jurisdiction ("OSJ Offices"). While some of these Offices are supervised directly by Home Office Principals, many are supervised by OSJ Offices. All of our Offices, including OSJ Offices are owned by registered principals and/or registered representatives, who have an independent contractor tax relationship with MSC. This is a similar business structure as that for most of the over 200 independent contractor broker-dealers who are member firms of the National Association of Securities Dealers, Inc. ("NASD').

I am the Executive Vice President and CAO of MSC and I appreciate the opportunity to submit comments on behalf of MSC concerning the NASD's proposal to adopt new NASD Rule 3012 and to amend other rules regarding the supervisory and supervisory control procedures of member firms ("Rule changes"). We believe that efforts to enhance supervision are important and that effective supervision is essential to investor confidence and efficient markets; however, we do not believe these Rule changes would be effective in enhancing supervision. In fact, we believe the implementation of some of these Rule changes may have the unintended effect of reducing effective supervision in many firms

Need for more NASD member input.

The Rule changes as proposed would have a serious negative impact on many small firms and on all firms that are organized on an independent contractor basis. The NASD membership includes hundreds of members that are structured differently than the large wire houses and regional firms and we do not believe these firms were adequately considered in the Rule changes. For the most part, these firms are not part of the "inner circle" that are informed on a timely basis about the need to comment on proposals made by regulators. For example, many are not members of the Securities Industry Association. Rather, they depend on the NASD to notify them of proposals and to ask for their input. Unfortunately, that process was completely skirted in this instance and many of those firms are completely unaware of the Rule changes and the potential deleterious effect on their business and cost structures. It would be highly unfair to implement the Rule change without adequate opportunities for those firms to know about it, thoroughly review it, and comment on it. Full review and thorough analysis of all ramifications of the Rule change on NASD members would also assist the Securities and Exchange Commission ("SEC") in assuring that supervisory rules are fair, balanced and meaningful. We urgently request that this proposal be sent back to the NASD with specific direction that they seek input from their standing boards and committees - including the Small Firm Advisory Board, the Independent Contractor/Insurance Affiliated Broker Dealer Committee and the Membership Committee - and from their full membership prior to asking the SEC's consideration for approval. We are certain the NASD meant well in determining to bypass these traditional channels; however, that decision combined with the short comment period provided by the SEC puts a significant number of NASD members whose operations are structured different than wire houses in a very vulnerable position with potential damage to both their supervisory structure and their financial stability.

Alternatively, if the SEC is not willing to send the proposal back to the NASD, we respectfully request that the comment period be extended to at least ninety (90) days so that all member firms (and particularly small and independent contractor firms) which desire to do so may comment after diligently and intelligently reviewing the proposal and its effect on their business.

Existing rules are adeauate

MSC believes that the proposed Rule changes relating to supervision of representatives are an overreaction to isolated failures by a small number of member firms. It appears to us that the Gruttaduaria case, which the NASD cites as the foundation for the proposed changes, resulted from one individual intent on stealing from customers and is not evidence of a general failure of the current regulatory system. In fact, if, as alleged, the firms involved with the Gruttaduaria case had complied with existing supervision rules it is possible the violations would not have occurred and it is almost certain that the amount of customer losses would have mitigated. Certainly no set of rules (including those being proposed) can fully protect the public against an individual or firm determined to commit fraud. However, we believe that current regulations are reasonable and sufficient when effectively implemented and enforced. The Rule change adds significant cost and complexity without meaningful enhancement of a firm's ability to detect the pattern of conduct illustrated in the Gruttaduaria case.

T Rule change is [illegible] i its present form.

Even if the SEC is convinced that additional rule making is needed to assure adequate supervisory systems, this Rule change does not accomplish that goal. The Rule change is imprecise and is needlessly burdensome. It will substantially increase costs for member firms without providing meaningful improvement in investor protection. Further, the Rule change may adversely impact implementation of recently released record keeping rules and rules responding to the requirements of the USA PATRIOT Act.

<u>The proposal is imprecise in language.</u>

Key words in various provisions of the proposed rules lack sufficient clarity. First, the heart of proposed Rule 3012 and the revisions to Rule 3010(c) is "independence". Rule 3012 contemplates independence of those persons charged with verifying compliance with firm supervisory procedures. Likewise, Rule 3010(c) requires independence from those charged with conducting branch office inspections. Unfortunately, there is no clear definition or explanation of "independent" as it is used in either proposal. To the extent that the term "independent" is the touchstone of these new rules it follows that defining this term is critical to a common and complete understanding of this rule. Failing to define such a key term leaves the rule open to inconsistent application within member firms and among the various **NASD** District Offices responsible for its enforcement. Similarly, changes to rule 3110 require record keeping with respect to the "essential facts" supporting an account name change. Again, no guidance is offered in the rule that illuminates the meaning of "essential facts." Such inarticulate rules unnecessarily require supervisors to make uninformed judgments about incomplete rules and handicap firms in development of meaningful compliance procedures.

<u>The proposal would create burdens without equivalent benefits.</u>

By introducing the concept of "independence" in the supervisory system the Rule change would, with a broad brush, scuttle proven effective supervisory systems for a new system that may not fit the geography, structure or function of a given firm. Worse, the system suggested in the Rule change is sure to require significant additional financial and human resources without any evidence that investors will be better served. This is especially true for independent contractor firms like MSC. For example, most of the Principals who oversee OSJ offices at MSC are owners of their own business including the Offices that report to them. Under the proposed rule those Principals would not be able to conduct (or supervise anyone else assigned to conduct) branch office examinations because they have an economic interest in those branches. MSC has found great value in requiring that Principals be personally involved in the branch examination process. It heightens their awareness of their role as supervisors and improves the examination process since these owner-Principals have the best understanding of the business structure and practices of the branches reporting to them. Thus the proposed rules would lessen the effectiveness of the supervisory process for MSC (and many other similarly structured firms). MSC still conducts annual compliance department inspections of all its OSJ Offices at least annually and attempts to visit all the other Offices at least every two years.

Further, the proposed rule would necessitate MSC's reorganizing its entire home office supervision oversight structure and hiring substantially more home office based compliance personnel to examine hundreds of branches currently examined by OSJ principals. Given the financial pressures inherent in the flat economy and sustained bear market, the firm would have no alternative but to schedule these branch exams on a multi-year cycle. In contrast the OSJ offices are currently required to do a full branch compliance audit and examination of Offices under their supervision annually. Again, in the case of MSC (and, we believe, most other independent contractor firms) implementation of the proposed rule would reduce effectiveness of supervision rather than enhancing it.

Independent review concept is questionable

The Rule change adds a requirement for an independent review of supervision systems. Adding a new layer of review doesn't make sense to us. To what extent should that independent review be subject to review as well? The rationale of the rule results in an endless chain of supervisors supervising supervisors, In contrast, the existing regulatory scheme requires that firms adopt policies and procedures reasonably designed to prevent and detect violations. That standard provides firms the necessary guidance in establishing a supervision system with specific goals in mind, but also provides flexibility for firms to create systems that fit their business and enhance their ability to supervise. Larger wire houses may believe that independent testing facilitates their living up to the standards of the existing regulatory scheme. If so, the current rules are flexible enough to permit adoption of independent testing. Other firms have already demonstrated the ability to create supervisory policies and procedures that are effective without an independent review. Further, mandating that all firms assign leadership for an internal independent review would soak up compliance resources currently assigned to other essential services, or would force firms to increase staffing during a period when most firms are being forced to lay off staff due to negative economic conditions. The NASD in its 19(b)(2) filing assured the SEC that this rule will have no significant impact on competition. We do not agree. We believe that the proposed rule, if adopted, will result in significant financial and structural harm to many small firms and to other firms, such as independent contractor firms, which are not patterned after wire houses. These firms will be less competitive structurally and financially if the proposed rules are adopted.

The Rule changes also create conflicts within Rule 3010, in our opinion. The existing rule 3010(g) establishes Offices of Supervisory Jurisdiction as those locations in which supervisory functions are performed. Obviously the rule presumes that those OSJ branches are to be staffed with managers and other registered persons with the responsibility and the expertise to effect supervision. The Rule changes appear to turn that presumption on its head by indicating that supervision through the examination process is only effective if done using independent parties.

Limited resources will be taxed.

As discussed above, we are concerned about the increased demands on resources that will result if the Rule changes are approved. For independent contractor firms like MSC, the Rule changes would severely reduce the number of MSC's Principals eligible to conduct Branch Office examinations. At the same time, the new branch definition rule (a separate proposal by the NASD) substantially increases the number of Branches for some independent contractor firms. The bottom line is that MSC and other independent contractor firms would have to hire additional staff and stretch our limited resources even further. Not all firms will have the economic capacity to make the difficult choice of increasing staffing during a recessionary period. When those firms face the need to send compliance employees to hundreds of additional locations, the duration and the quality of the audits will likely decline. Furthermore, the audit cycle will lengthen, increasing the period of time between inspections. Accordingly, the proposal may have an unintended result, forcing firms into economic dilemmas that erode supervisory resources without any evidence that examiner independence will improve supervision outcomes.

Structural issues relating to independent contractor firms.

MSC has actively sought to make supervision timelier, more hands on and as close to the point of sale as possible. We believe that the closer the supervisor is to sales practices the more effective they are at identifying problems quickly and taking prompt remedial action. To support these efforts MSC has invested substantial resources in training its OSJ owner/managers to equip them for their supervisory role including doing branch examinations. This model, which we believe to be effective in protecting and serving client interests, is directly attacked by the proposed rule.

MSC believes the Rule changes, including the requirement that Office examinations be separated from the sales supervision function, will have a negative impact on the corporate structure of hundreds of independent contractor member firms. Along with the majority of such firms, MSC employs a hierarchical system of supervision. Many of our Representatives work in non-OSJ Offices, most of which are assigned to an OSJ Office for supervision. The OSJ Manager is also responsible for an annual inspection of each office under his/her supervision. In addition, each OSJ Office is supervised by home office based, salaried Principals and is inspected at least annually by home office based, salaried compliance personnel.

To divorce the inspection of Branch and satellite offices from the supervision of the Representatives assigned to those locations is to introduce an artificial distinction between the two activities. We believe that our OSJ Managers, who are most familiar with the Representatives and activities associated with those locations, are the most qualified to perform the periodic inspection. The increased understanding gained fi-om the inspections enhances the effectiveness of the OSJ Managers' supervision and the supervision activities provide additional information regarding the types of activities that should be more closely monitored in the inspection. In addition, when **OSJ** Managers inspect the Offices, it serves to reinforce the **OSJ** Managers' accountability for their Representatives' actions. By appointing an outside party (such as the firm's Compliance Department or unrelated contractors, as many small firms will be required to do) to audit the Branch and satellite offices, OSJ Managers will have a decreased sense of responsibility with regard to the activities conducted at the offices.

Currently, our OSJ Managers understand that in the event of wrongdoing by a Representative, the OSJ Manager will be held accountable by the firm and its regulators unless he/she is able to demonstrate effective supervision over the Representative. The NASD's proposal may lead some OSJ Managers to feel that their supervision is less important, as they begin to rely on the firm's Compliance Department to detect problems during the periodic office inspections. In essence, the overall level and quality of supervision over the Representatives may decline.

The proposal may result in implementation delays for other key rule changes.

As stated above, the Rule changes would add significant human resource and financial costs to our Compliance Department. Our firm is awaiting guidance from the Treasury Department on customer identity verification. In addition, the firm continues to work on the implementation of the SEC's revised requirements for the maintenance of books and records. Even with increased funding for supervision, there is a limit to the amount of change that may be implemented to our systems at any one time. Because the office examination process is a core component of our supervisory structure, changes in this area will impact the timeline for completing changes in these other key areas.

We strongly believe that by barring the firm from making appropriate use of its OSJ Managers, the proposal will result in decreased supervision of our representatives and a waste of the resources allocated to supervisory and compliance functions.

Provision for exemptions.

The argument might be made that the NASD provided in the Rule changes that a member could be exempted from the independence requirement for office inspections if they can demonstrate that complying would be unduly burdensome and that the members current inspection procedures are reasonably designed. However, we are certain that it is not the intent of the NASD to review hundreds of exemption requests and grant them. Yet that is what the scenario would be if the Rule changes are adopted as proposed, since virtually every independent contractor firm would face enough personnel and financial burden to justify such a request. If one includes small firms, which will also find it difficult to comply with the Rule change, then a majority of NASD member firms would be requesting exemption. Exemption provisions only make sense if they are provided for unusual situations. In the case of this Rule change proposal, the wide range of firms that will have serious issues dictates a careful review of the underlying Rule rather than reliance on requests for exceptions.

Effective dates.

This Rule change is set on a fast track and that that may cause significant problems in implementation. If the Rule change is not sent back to the NASD or the comment period is not extended, the Rule change could be approved by the SEC early in January. The NASD has stated that the effective date will be announced in a Notice to Members to be published no later than 60 days following Commission approval and that the effective date will be 30 days following publication of such Notice to Members. Bottom line is that the Rule changes could be effective as early as 60 to 90 days from now. MSC would have to completely re-organize its supervisory structure, re-write significant portions of its supervisory and office inspection manuals and guidelines including designing and documenting an entire new testing procedure, recruit and train additional compliance staff members to do branch office examinations, retrain both certain staff members and OSJ Principals and design and program any changes in its data processing systems to accommodate all these changes and the new books and records rules contemplated under Rule 3110 (d). we are not miracle workers. We assume these potential time frames will prove impossible for many firms to meet as the industry is already scurrying to make the systems and process other mandated changes, including the revised books and records rules and the requirements under the USA PATRIOT Act. All these have been piled on during a period when the markets and economy have forced broker-dealers to be extra frugal, while still maintaining strong supervisory and compliance systems. We are not miracle workers and we need a reprieve from this flurry of change.

Summary and conclusions.

At our firm, similar to many of our peers, the Chief Compliance Officer ("CCO") is responsible for the design, implementation and oversight of the firm's system of supervisory controls. Restricting the CCO from performing and/or overseeing such a review would compromise the quality and thoroughness of each review. *An* alternative to fulfill the new independence requirements would be to assign someone from Marketing or Operations to perform the review. This approach may be effective in wire houses where salaried branch office managers and operations managers are common. Since MSC and other independent contractor firms do not have Marketing and Operations personnel resident in OSJ branches, we believe that such an alternative would likely result in a supervisory review that is less sensitive to securities compliance issues.

Finally, given the relatively small number of serious cases, as compared to the universe of firms and representatives, it appears that the majority of firms clearly strive to conduct business in a manner that is compliant with industry rules and regulations. Members realize that if the public loses faith in the investment community, then we all lose. We are confident that the current regulatory environment already provides the necessary tools and resources for firms to properly oversee their Representatives, and we strongly believe that the Rule changes will actually have a negative impact on the effectiveness of our overall supervision. At the same time the Rule changes would place a significant financial burden on NASD members.

If strictly construed, the proposals would establish new requirements that could be extremely burdensome for firms, particularly small firms, to implement. The proposed rule changes present a huge burden for independent contractor firms and firms with far-reaching branch networks. For the reasons cited above, the Rule changes it relates to independent inspections of branch offices would have been more appropriate as a recommended guideline for effective supervision rather than a hard and fast rule that applies to firms across the board. MSC strongly urges the SEC to consider the real world ramifications and costs of this proposal and to consider alternatives that would allow firms to meet their obligations with internal resources and minimal disruptions to existing supervisory structures.

Again, we appreciate the opportunity to comment on these important issues and request that the time allowed for comment be extended to at least ninety (90) days to accommodate many firms that have not received timely notice of the Rule changes and have not the opportunity and/or the time to respond.

Sincerely,

Dennis S. Kaminski
Executive Vice President/CAO

DSK:lgw