September 22, 2004

BY ELECTRONIC MAIL

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

Re: File Number S7-25-99 — Certain Broker-Dealers Deemed Not To Be Investment Advisers (Release No. 34-50213, August 18, 2004)

Dear Mr. Katz:

Northwestern Mutual Investment Services, LLC ("NMIS") appreciates the opportunity to comment on proposed Rule 202(a)(11)-1 under the Advisers Act and related changes to Form ADV.[1] NMIS was organized in 1968 and is wholly owned by The Northwestern Mutual Life Insurance Company. NMIS offers a full range of securities products and services and is registered with the Commission as a broker-dealer and as an investment adviser.

We strongly support the rule proposal. Giving investment advice is a core component of the services our broker-dealer representatives offer, as it is for most firms that make personalized recommendations as part of their broker-dealer business. The flexibility to price these services on other than a per transaction basis allows us to better meet the needs and preferences of individual customers.

In the release inviting additional comments on the rule proposal, the Commission asked whether current fee-based programs more closely align the interests of investors with those of brokerage firms and their registered representatives than do traditional commission-based services. In our view, the answer to this question is that such programs are appropriate in many cases for exactly this reason.

As noted in the Tully Report nearly ten years ago, "the prevailing commission-based compensation system inevitably leads to conflicts of interest among the parties involved."[2] Although the Committee also found that commission-based compensation works remarkably well for the vast majority of investors, it also identified offering fee-based brokerage accounts as a best practice:

> ***Payment for client assets in an account regardless of transaction activity.*** In many cases the best advice an RR can give a client at a point in time is to "do nothing," or to keep assets in the safety of a money market account. The RR's

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[1] Certain Broker-Dealers Deemed Not To Be Investment Advisers, Exchange Act Release No. 34-50213 (August 18, 2004) (reopening of comment period) and Exchange Act Release No. 34-42099 (November 4, 1999) (proposed rule).

[2] Report of the Committee on Compensation Practices, [1995 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,614 at 86,509 (April 10, 1995).

> reward for this advice is zero compensation. Some firms' practice of basing a portion of RR compensation on *client assets in an account* is seen as one way to reduce the temptation for income-seeking RR's to create inappropriate trading activity in an account.[3]

While we recognize that no compensation arrangement is a panacea for conflicts of interest and that fee-based accounts are not appropriate for everyone, nothing in our experience suggests that the Tully Report in general, or this conclusion in particular, should be repudiated.

In the release inviting additional comments on the rule proposal, the Commission also asked what the practical impact on broker-dealers would be if the Commission determined not to adopt this rule as proposed. In our view, withdrawing the rule proposal without action would create a great deal of needless confusion among our customers and costly uncertainty in the financial services industry.

Fee-based programs have become very popular in the five years since the Commission issued the proposing release. A substantial number of fee-based accounts have been opened during this period. Many of these account relationships could be disrupted if customers must be told their preferred pricing plan can no longer be made available due to a change in regulation. Customers who value the fee-based account option are likely to view this kind of regulatory change as something less constructive than investor protection.

Merely treating existing fee-based accounts as advisory accounts is not a realistic solution either, even for a broker-dealer that has already registered as an investment adviser. If fee-based accounts are determined not to fall under Section 202(a)(11)(C) of the Advisers Act, broker-dealer representatives servicing fee-based accounts could be subject to licensing by the states as investment adviser representatives.[4] In some cases, the additional license would take time to obtain because of additional examination requirements (the Series 65 or Series 66, for example). In the meantime, the account would likely have to be reassigned. Our account relationships have an important personal dimension, and registered representatives are not fungible.

The Commission also asked whether broker-dealers who would seek to rely on the rule should nevertheless be required to register if they market fee-based accounts based on the quality of investment advice provided. Although we agree that investors should be informed that fee-based brokerage accounts are not advisory accounts and we support disclosure requirements to this effect, it is not at all clear how the Advisers Act and the rules thereunder would apply to a broker-dealer that registered as an investment adviser solely for advertising purposes. Moreover it is entirely unnecessary. Broker-

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[3] Id. at 86,511.

[4] Section 203A(b)(1)(B) of the Investment Advisers Act preempts the application of certain state investment adviser regulations to persons excepted from the definition of "investment adviser" under Section 202(a)(11).

dealer firms are already subject to NASD advertising rules, which are much better developed than advertising regulation under the Advisers Act.

More importantly, the accurate usage of terms such as “investment advice” and “financial planning” should not be prohibited. If broker-dealers can engage in activities fairly described by these terms, there is no good reason to prohibit them from using these terms in their public communications, including advertising. Such a prohibition would likely result in the development of new vocabulary that would be more likely to confuse investors about the services they are getting than it would be to inform them.

The proposed rule is in the public interest because it increases the choices investors have to get the advice they need and to pay for it in the way they prefer. We urge the Commission to adopt it.

Thank you for the opportunity to comment. If you have any questions, please call me at (414) 665-5034.

Very truly yours,

Mark A. Kaprelian
Secretary

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