

February 26, 2006

I write on behalf of the [International Association of Small Broker Dealers and Advisers](#) to comment upon the above referenced proposal. Whatever the intention or merits of the new SRO gift policy, allowing firms to use their discretion, will be impossible to enforce because the NASD lacks jurisdiction over those those clients accepting the gifts. Even if it had jurisdiction, why would any client ever acknowledge that its decision-making was or could be influenced by gift giving. That there have been very few disciplinary actions under the current objective standard suggests that it should not be made harder to enforce or surveil with a subjective standard. Compliance surveillance will pit the compliance department against the business side in arguing over whether how much is too much and whether it might actually influence the client's decision-making. Finally the determinant for a violation i.e. whether it will be likely to cause a customer employee to act inconsistent with his employer's best interests is too subjective to be practical. The compliance department has to determine whether a pattern of business entertaining is likely to cause a customer employee over which it has no control to act inconsistent with his employer 's interest regardless of whether he ever did or in fact whether any business was done. This subjectivity can only cause internal strife within the firm's compliance business structure unless the firm establishes a fixed amount of spending. If it does, it will have to be similar to its competitors. The end result can only be a large amount for big firms who can afford such expenditures.

The policy therefore clearly works against the small NASD member firms as discretion will create an upper bracket that allows for Bordeaux in New York and a lower bracket for the the small firms who can only afford Merlot. Limiting individual gifts to \$500 and \$750 in NY City will allow reasonable entertainment everywhere and place the firms on a more equal footing. After more than 30 years of limiting gifts , this change is a highly unusual effort to make NY City style entertaining reasonable and available, but only for those who can afford it. The suggestion by senior SRO personnel that you can't buy dinner in NY for \$500 suggests that this policy was clearly developed by Wall Street firms wanting the freedom to justify Wall Street entertaining and this new concept certainly leans toward a more flexible policy that may not be enforceable. The proposal can however be easily modified as follows:

- All of the large firms have dining rooms where clients can be entertained and the proposal should apply there.
- Educational, charitable and philanthropic events where firms are expected to buy a table are good venues for the proposal as they are very public and serve a genuinely good non-business purpose.
- Closing dinners that include a large number of client personnel are valid items for the proposal as they are rewards for work done and are also transparent to senior management in both entities.

The proposal however especially discriminates against small firms when it comes to one on one entertaining of senior personnel of the client. Whether its a dinner, sporting event or other entertainment, these rendezvous can have only one purpose, which is to influence the judgment of the person being entertained in a non-public way. There are many alternatives to the proposal for these situations.

- many cost of living indexes are available so that NY could have a higher limit than the smaller cities
- yearly entertainment above \$500 could require subsequent audit committee review
- a yearly report of such extra-entertaining could be sent to the firm's sro co-ordinator

- such extra entertainment should require a written explanation by the provider of exactly which client business it is intended to attract.
- a temporary trial among a limited number of firms would give the NASD a better concept of how these policies will look and work in practice. The voluntary efforts of the Derivatives Policy Group is a good precedent for this

Surely the NASD understands that much of the business this entertainment is designed to attract, has become commoditized. Commissions for institutional trading including options and futures are so low that entertaining a hedge fund or mutual fund manager must be intended to give the entertainer an edge over its competitors and those who can entertain the most are more likely to get the business. This puts the small firm at a disadvantage especially when the big firm is spending shareholder money. The investment banking business is distinguishable but it must be recognized that it is an oligopoly already controlled by 10 firms. Perhaps those firms should disclose in the prospectus the amount of entertainment they needed to get the mandate. The important point is that the small investment banks have enough of a challenge without having to compete on entertainment. It can only be good for competition if the entertainment factor exists on a level playing field. Finally, as has been noted in recent news stories, business entertainment can be discriminatory in nature whether in a stripper bar, private club or sports event. The industry does not need more flexibility to entertain in such fashion. As both the medical profession with respect to drug sales and Congress with respect to lobbyists, tighten the reins on gifts, the securities industry should not give the appearance of loosening. Finally abuses will require proof of a bribe or an attempt to bribe a person over whom the NASD has no jurisdiction and secondly that the firm knew or should have known the bribe occurred. The client and its employee will never acknowledge it was bribed. The compliance department will find itself arguing with the front office as to whether a \$1000 birthday dinner between friends was appropriate and whether it could unreasonably influence the judgment of someone they have no control over. As indicted above a pilot program for such discretionary policies will educate everyone regarding the challenges discussed herein.

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