Statement of Electronic Traders Association
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Hearing Before the Permanent Subcommittee on Investigations
Committee on Governmental Affairs
United States Senate
Washington, D.C.

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I.

Introduction

The Electronic Traders Association ("ETA"), a non-profit trade association of on-site day trading firms,[1] is grateful to the Permanent Subcommittee on Investigations ("Subcommittee") for this opportunity to dispel various misconceptions which have arisen concerning day trading. Knowing of the Subcommittee's interest in promoting the interests of small investors we appreciate also the chance to inform the investing public of the many benefits small investors derive from other individuals willing to accept the responsibility of risking their personal capital in day trading.

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[1]ETA, founded in 1996, has approximately 15 supporting organizations, including six of the ten largest on-site day trading firms. ETA members service customers who are a majority of active day traders and execute a majority of day trading transactions.

In common with all innovators, electronic day trading has been considered a threat to the established order, and has been under attack for years. In the nineteen eighties the handful of firms involved were maligned by market makers and regulators as "SOES Bandits". Today, the charges are, alternatively, that day trading is gambling or that (presumably to even up the odds) day traders routinely violate the securities laws.[2] Day trading is not gambling, it requires skill, state of the art technology and hard work.[3] And, from published decisions, it is clear that the record of day trading firms complying with securities laws is better than that of the 100 largest broker-dealers (see Appendix A).

Although on-site day trading has developed greatly, electronic day trading firms are by securities industry standards, tiny. ETA estimates that there are 62 on-site firms, of which 10 do 80% of the business, and somewhat less 5,000 full-time professional on-site day traders (including a small number of individuals who trade remotely through on-site firms locations via dedicated telephone lines). However, ETA also estimates that these individuals, trading an average of 700 shares, 35 times a day and almost entirely in the most liquid Nasdaq stocks, trade the equivalent of 15% of Nasdaq volume daily, and comprise the largest portion of retail limit orders in the major Nasdaq stocks.

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[2]"[D]ay trading firms... need to play by the same rules the rest of Wall Street follows. If they don't get their act together they will be under increasing regulatory pressure." Peter C. Hildredth, NASAA Press Release, August 9, 1999.

[3]"Dan Ripoll is sick of reading stories criticizing his career of choice. 'The people writing [these stories] don't have any idea of what we do,' he says. 'This isn't gambling.' " HTTP://CNNFN.COM/1999/09/01/INVESTING/DAYTRADE_DAYINLIFE/.

Day traders understand that they are accountable for their decisions. Those decisions and the trades they make are theirs alone. And they are therefore accountable for the money they make or lose. ETA members however, emphasize that day trading is not for everyone. And ETA believes its members are both responsible for informing day traders about the risks of such trading and avoiding all hype about possible rewards. It has apparently not been recognized that the vast majority of ETA members' day trading prospects are references from customers, only a small fraction of whom are accepted. In fact, as the New York Times reported, "many former professional traders, brokers and financial service professionals are quitting their jobs to work full time as day traders..."[4] Nearly all day traders are college graduates and many hold graduate degrees.

On-line day trading differs from on-site trading. On-line traders, estimated to number more than 250,000 individuals, using firms such as Charles Schwab, Fidelity, E*Trade, et al., trade 1 to 3 times per day. They have been insightfully referred to by Chairman Levitt as "Day Traders Lite". The business of on-line traders is eagerly competed for by the major on-line discounters. As a consulting group recently reported, "on-line leaders... are about to enter a bloody fight for customers".[5]

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[4]The New York Times, August 13, 1999; also see footnote 3 "Ripoll quit Merrill Lynch's market-maker training program a year and a half ago to day trade."

[5]Forrester Research, May 11, 1999. See also, among many, advertisement in New York Times, Discover Brokerage, "Gordon Gekko Eat Your Heart Out", August 1, 1999, Business Section, page 9 (reproduced as Exhibit B). (On-line firms are expected to spend over $1.5 billion for marketing in 2000.)

Although the technology available to on-line traders continues to improve, it is not the equal of technology available to on-site traders. Please note three important differences between on-line and on-sight day traders:

First, at an on-site firm, the customer is connected directly to the firm's order router; trading through an on-line firm the customer's PC has no direct connection to the firm's order-router. This adds perhaps a second to the order entry process; in day trading seconds are expensive.

Second, because of on-line brokers preferencing arrangement with market makers, on-line traders do not have the opportunity to receive price improvement on their orders; on-site firms' technology offer access to all ECNs and markets.

Third, on-line traders trade in isolation from other traders; thus they can not access the intellectual capital provided by other day traders which is available at on-site firms.

The growth of on-site day trading and day traders is, at this point, almost primarily due to: a stock market with consistently high volume; extraordinary technology which is equal to or in advance of that available to securities industry professionals, the SEC's recently enacted order handling and alternative trading systems rules and the entrepreneurial culture, emphasizing personal responsibility, which has renewed its strength in this country over the past two decades.

II.

Day Trading Business Standards

ETA members are SEC and state registered broker-dealers; nearly all are members of the NASD which introduce their business to clearing firm members of the New York Stock Exchange and NASD. ETA members are reviewed regularly by the NASD; most have been visited by the SEC in its "sweep" of day trading firms. So far as we are aware, only one ETA member has ever been the subject of SEC or NASD discipline (which resulted in a $7,500 fine for order entry violations), and no ETA member is a subject of an SEC or NASD proceeding. Given the fact that most on-site day trading firms have only been in existence for a few years, their procedures are continually being refined. Whatever failings a few state securities regulators may cite are relatively minor, and these failings, as Exhibit A shows, are certainly not unique to the day trading business.

On a positive note, ETA members seek to meet all regulatory requirements. They seek to foster high standards of ethics. Thus for example, ETA's risk disclosure statement (Exhibit C) adopted in February 1999 not only reflects the risk disclosures proposed currently by the NASD, but also points out such additional risks as the possibility of loss through systems failures, inability to liquidate positions because of market conditions and the lack of ultimate safety in stop-loss type orders. The ETA form also requires, as the NASD proposal does not, that the prospective day trader execute the risk disclosure form acknowledging his awareness of the risks of day trading. Disclosure of risk is simply not an issue.

ETA members promote the importance of being fully forthcoming regarding each firm's traders' successes and failures, and offering prospects access to those traders to conduct their own due diligence. As a matter of business ethics, ETA's Statement of Principles (Appendix D), does not permit exaggerated statements regarding possible trading results.

The NASAA report characterizes day trading in the view of on-site firms as a program or strategy of investing. Better said, day trading is an approach to the market characterized by multiple trading strategies. Under such circumstances, where traders hold positions for four minutes and make their own decisions, the concept of suitability, even repackaged as appropriateness, has no meaning. A day trader, in thirty market days, will make more than 2,000 buy/sell decisions; in ten days, 500 trading decisions. At what point is the day trader considered sophisticated enough so that suitability can not possibly be an issue? After all, most investors, including those deemed sophisticated, do not make 500 trading decisions in a lifetime, let alone 2,000 decisions. Accordingly ETA believes that the NASD proposal currently before the SEC is too general in nature to be useful to regulators, firms or customers. However, while, as noted, ETA does not believe in a suitability standard for on-site day trades, if in fact there is to be such a standard ETA for the reasons described below considers that NASD Rule 2860, which governs procedures used for opening retail option accounts, furnishes a better model.

Option trading, like day trading, is an approach to the market composed of many possible strategies bearing lesser and greater degrees of risk. Under Rule 2860, an individual trading options, receives a risk disclosure statement, signs a new account form verifying that the information he has provided regarding his finances and market experience is accurate, and then based on this information is initially allowed to trade, as suitable, the spectrum of available strategies. This sensibly is a one time analysis, and under the Rule (¶19) suitability applies only to recommended transactions. At ETA members, beginning day traders, without previous experience generally are limited to strategies such as trading on news or momentum, with limited size and leverage, as compared to experienced traders who can accept the riskiest strategies of leverage and positioning.

III.

Misconceptions About Day Trading And The NASAA Report

Rather than burden the body of this statement with a point by point refutation of a number of misconceptions promoted by the NASAA Report about day trading we address these misconceptions in Appendix E. However, two causally related misconceptions, that day trading firms advertise falsely to obtain customers and that all, but a tiny fraction of day trading customers will lose all their money, demand immediate response even though the educational level of the prospect and customer base noted above should be in itself enough to show their absurdity. With deference, we believe that without these claims it is unlikely that this Subcommittee would consider these hearings useful.

The first claim, deceptive advertising, endlessly repeated, appeared most recently in a statement by Matthew Nestor, the Massachusetts Securities Division's Director, who noted that Massachusetts' investigations did not stem "from customer complaints but from concerns about on-site firm advertising".[6] The second, the allegation that there is an extremely high percentage of customer losses, appears in its most recent formulation in the NASAA press release concerning its August 9 1999 report:[7]

These related themes of losses hidden from customers have been pervasive in NASAA's approach to this issue.[8] That this approach is driven by NASAA's desire for publicity was clearly stated by NASAA President Peter C. Hildredth in his remarks to NASAA's winter enforcement conference.

> "I think we need to reposition ourselves... Another way to tell our story is to ... be more visible... by cultivating media contacts. <u>The news media is hungry for good crime stories - and with a little imagination we can find them stories to write about</u>."[9] (Emphasis added.)

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[6]The Atlanta Constitution, August 18, 1999.

[7]Report of the Day Trading Project Group (hereinafter "NASAA Report").

[8]We note NASAA, but in actuality, it is a task force of states; in fact, only four states have brought actions against day trading firms, and only one state, Massachusetts, the author of the NASAA Task Force Report, has for whatever reason conducted a major campaign against on-site firms. Conspicuously absent are major financial states such as New York, California, Illinois and Florida. New York, the most sophisticated of the blue sky regulators, as a result of on-line customer complaints, has focused entirely on on-line firms.

[9]Remarks, Miami, Florida, January 11, 1999.

Thus NASAA's "imagination" that day traders lose money in wholesale numbers. Lacking analytical proof NASAA commissioned a "study" of day trading results. That study, is hardly convincing. Despite NASAA's claim that its analysis "was resource intensive", with "thousands of entities "reviewed, the analysis itself is based on only 17 accounts, which on average traded for four months, at one office of one (now ETA) firm, at least two years ago. It does not add to the strength of the study that it has been conducted by a retired commodity trader operating out of his apartment who makes his living as a witness for plaintiffs in commodity cases. Nor does it add to the "expert's" credibility that his resume (See Exhibit F) lists with pride both that he "published daily hot line trading recommendations" and that as an investment advisor (apparently unregistered) he "developed [a] low price stock strategy that returned over 30%".

The NASAA report is also the home of a number of contradictory thoughts: one example, is a discussion of a study by two California business professors ("Short Term Trading is Injurious To Your Wealth"), which, in fact, shows that short term traders while they underperform the Dow-Jones Index (in common with mutual funds, as the study points out), <u>make</u>, rather than lose money; however, the period studied is 1991 - 1997 and the commissions charged to customers were ten times those now prevailing. If such present commission structure were factored in, the accounts presumably would well outperform the Dow-Jones. Another example, the claim that there is an inherent flaw in day trading theory since, as NASAA views it, only by letting profits run can traders make money, a claim that is contradicted by its expert's report which adopts the opposite view that it is the holding of positions overnight that leads to the "risk of ruin".

It is interesting to note that the NASAA Report ignores a study of Professor Paul Schultz (the individual almost single handedly responsible for exposing collusion in the Nasdaq market place) which found day trading to be a successful market approach. His comment about day traders was that: "On average, they made money, but because of the reaction time of a trader is very rapid, it's a game best left to young people with good memories."[10]

However, much of the NASAA Report's this mumbo jumbo would be unnecessary if NASAA had accepted ETA's March 1999 offer to provide current trading information. (NASAA's response was that it would "reserve comment on the proposed survey".) Apparently recognizing that it is undisputed that a high percentage of accounts lose money as they advance on the trading learning curve (which ETA believes runs three to five months), the NASAA study followed the principle that these accounts, would not profit from experience, but merely by day trading would have a "risk of ruin". One needn't be a graduate in statistics to understand that the study's results, and the NASAA claims (depending on the occasion) that 7 or 8 or 9 out of 10 on-site day trading customers lose money, are absurd.[11]

The NASAA Report also claims that there is a high turn over of customers. If in fact 3,500 - 4,500 of the 5,000 day traders were wiped out every six months or so, there would be by

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[10]Quoted in article cited in footnote 3. On the other hand, one ETA member surveying its customers, found their average age to be 37. (The survey also found previous customer average income of $120,000 and net worth of $600,000.)

[11]"[R]egulators say that nine out of every ten trades lost money." Newsweek, August 8, 1999, p. 30.

now at least 20,000 individuals who had lost in the aggregate hundreds of millions if not billions of dollars. One would therefore expect complaints by the hundreds if not thousands. That few or none have been brought to Mr. Nestor's office, nor, judging from the silence of the NASAA report on the subject, anywhere else, is the clearest evidence that the NASAA loss numbers are unconvincing and that disclosure of risk is not an issue. Presumably it also explains why there have been no regulatory actions brought against day trading firms by the vast majority of NASAA members (including such giants as California, New York, Illinois and Florida).

Earlier this year ETA informally surveyed certain of its members to obtain a rough estimate of customer profitability. These estimates were that after an initial period of three to five months of losses 60 - 65% netted in the range of $28,000 per month, with the balance of customers losing $6,000 - $8,000 per month. In August, ETA's Executive Committee members considered these numbers still to be representative. Please note that these are only estimates, unlike the NASAA Report, they do not purport to be scientific. To put the matter to rest, ETA is in the process of retaining KPMG to conduct a day trading profitability study; this study is expected to be completed in the next two months.

IV.

How Day Trading Benefits The Investing Public

These are the ways the average investor - who may never short term trade, let alone day trade - benefits from the activities of on-site day traders.

Transparency

Until a Justice Department investigation and action by that Department and the SEC, there was substantial evidence that market makers conspired to keep price quotations artificially wide. ECNs, the trading systems fostered by day trading, have forced competition upon market makers. Quoting Traders Magazine: "The number of ECNs exploded on Wall Street soon after the implementation of the order handling rules. This caused market makers to make their price quote information more transparent and to improve their handling of retail size limit orders." Most importantly, ECN prices are driven by actual orders, while Nasdaq is a market of quotes by dealers. There is, as a result, more competition now for market makers than has ever existed before.

Until 1998, Instinet, an ECN which, as its name implies, is aimed at institutions, had a virtual monopoly on trading in this third market. Thus, institutions (and market makers laying off excess positions) could deal anonymously through this back door to Nasdaq receiving better prices than were generally available to individuals. All attempts over the years to create other successful ECNs had failed for lack of liquidity. Only when on-line discount and day trading blossomed did ECN competition become meaningful. By December 1998, the volume of one ECN, Island, was nearly equal to Instinet's. A key factor behind Island's success is the order flow of the major day trading firms. Thus day traders helped break the market maker trading monopoly and provide an obvious public good to all investors.

Liquidity

The New York Stock Exchange has found that individual investors have greatly increased their presence in stock market activity, and that for the first time in a generation individuals rather than institutions were the major traders in such well known stocks as Dell Computer, Cisco Systems, Lucent Technologies and Compaq Computer. Forbes Magazine, looking back at 1998, reported that block trades (10,000 shares or more) had dropped below 50% of market volume. A large part of the reason is given by an institutional trader: "Individual traders now have a lot of the same tools we institutions do; real-time quotes, push button executions..." Day traders add prodigiously to the depth of the market and its liquidity. Liquidity benefits every investor.

Reduced Spreads

ETA estimates that limit orders constitute nearly one-half of day trader orders. Since the vast majority of all customer orders are at the market, these limit orders disproportionately improve prices. Limit orders provide price competition to market maker quotes, shrinking price spreads and thus reducing trading costs for the benefit of all investors. In simple terms, if a market maker is quoting a stock at 50-50-1/4, a customer limit order at 50-1/8 will efficiently narrow that spread.

In addition to reducing spreads the SEC correctly believes that limit orders would benefit the public by increasing quote competition, thus enhancing the price discovery process. Please note that beyond executions, the key consideration is to present to the public an accurate picture of trading interest. In fact, it has been noted that, since the National Best Bid and Offer (NBBO) is the starting point in negotiating execution prices with institutional investors, narrowing the quoted NBBO improves the quality of executions for both retail and institutional investors (who are, of course, proxies for individual investors).

Other Benefits

The fostering of new hardware to transmit information and accelerate executions, whether in the form of broadened telephone lines or more efficient servers and routers, results in technological benefits to the larger economy. Perhaps most importantly, removing the middleman broker in choosing securities, and pressing competition on self-regulatory organizations, means an enormous reduction of the need for ethical sales practice regulation, eliminating traditional concerns about churning, mark-ups, trading ahead of customers and the like. In fact, the savings should even allow blue sky regulators to focus on the real problem of Internet fraud, rather than imagined problem of day trading.

V.

Day Trading Firms are a Desirable and Integral Part of the Securities Industry.

For the above reasons, major financial interests have invested in day trading firms and those who provide services to them. Softbank Corp. (which owns 26% of E*Trade and is the largest shareholder of Yahoo) and J. W. Childs have taken large stakes in Tradescape, a day trading software firm which is acquiring Momentum Securities, one of the largest day trading firms. The Texas based Bass family invested $40 million in TradeCast, a firm that makes day trading software, and a Bass representative will sit on the Board of TradeCast.[12]

These investments provide a number of insights to the Subcommittee: first, the investments reflect the restructuring of financial markets now taking place; second, each investment was made after considerable due diligence by the investors - had such review shown violative conduct the investments would not have been made; and third, the investments indicate, that day trading is in fact just another (albeit growing) facet of the securities industry.

Further evidence of the above appears in an August 13, 1999 New York Times report that Fidelity Investments, Lehman Brothers and Instinet are considering "adopting the software platforms of day trading firms, forming alliances with them or making outright acquisitions..." These firms' interest is in technology and transaction volume.[13] As the article puts it, "Electronic Communication Networks are gobbling up a growing share of the marketplace and firms want to make sure they do not miss out".

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[12]Dow Jones News Service, August 25, 1999.

[13]See also: "Wall Street Warms Up to Day-Trading Brokerages", the Los Angeles Times, July 14, 1999.

Two points derive from this.

1. As we have noted in the preceding section, volume is necessary to make ECNs effective (each of the firms named in the New York Times article has an interest in an ECN). A recent article in "The Industry Standard", a publication which follows Internet developments, notes:

> "You can't run a stock market without people who want to trade. That issue confronts the growing group of ECNs, which offer active stock traders an alternative to the big stock exchanges. Theoretically, ECNs offer a more efficient way to trade stocks. For the systems to gain traction, however, they need to attract a critical mass of users. It's a chicken and egg problem: it takes liquidity to attract liquidity.[14]

2. Wall Street firms exist in a world of myriad regulations; they expect regulation and discipline. As noted in Appendix A, from January 1, 1998 forward no fewer than 50 of the SIA's 100 most well capitalized broker-dealers, including such well known firms as Merrill Lynch, NationsSecurities, Piper Jaffray, Hambrecht & Quist and Prudential Securities, et al. have been disciplined by regulators (some more than once) for the kinds of violations which are the inevitable detritus of brokerage activities. The charges are exactly the kinds of allegations against day

[14] The Industry Standard, July 12, 1999.

trading firms made (in magnified fashion) by the NASAA Report; that is, order entry matters, short sale, margin and books and records violations, as well as failures to monitor trading practices and register personnel; even omissions as to the risks of investment losses and false marketing. The institutions investing in day trading firms realize that the alleged violations are within the pattern of regulatory discipline; that is, fines reflecting the seriousness of the offense and the firm's capital, and measures which stress the importance of corrective actions, proper supervision and compliance.

Summary

All participants in the securities industry respect securities regulators. In this regard, ETA believes that it is significant that to this point, neither the Securities & Exchange Commission, nor the NASD, have initiated disciplinary action of any extraordinary nature against on-site day trading firms. Thus the evidence is convincing that the attempt to demonize day traders has been orchestrated by a small group of NASAA officials for their own purposes.

Day trading is not gambling. The majority of those who day trade after training do not lose money. The individuals who day trade represent the democratization of securities trading. They neither seek nor need the protection of regulators. Their lack of complaints in itself speaks volumes.

More importantly, day trading provides great benefits to the economy and to small investors everywhere. If it were not for day traders, history tells us that competition by ECNs with market makers would either be weak or non-existent. If it were not for day traders market maker spreads would be higher than they are at present. If it were not for day traders, the technology of the securities industry would not have advanced to its present level.

Day trading firms are part of the securities industry. That fact is recognized by the large investments in them made by institutional investors. Those investments would not be made if day trading firms were wantonly violating securities regulations. Current regulatory cases show that the majority of major broker-dealers have been the subject of discipline by regulators for activities similar to those alleged of day trading firms.

ETA members seek to be in compliance with all regulations; they promote risk disclosure and avoid hype. While ETA believes suitability standards are out of place in a business where investment decisions are made dozens of times a day independently by customers, it also considers that if there is to be a suitability standard, the option rules provide a useful model.

Appendix A

Disciplinary Actions

January 1, 1998 - August 31, 1999

(SIA Top 100 Firms By Capital)

Date	**Firm**	**Violations**	**Penalty**	**Regulator**
02/98	Raymond James	Books/Records Sup.	$ 35,000	NYSE
02/98	Mayer & Schweitzer (Schwab)	Trading Violations	29,000	NASD
02/98	Troster Singer (Spear Leeds)	Customer Order Violations	198,000	NASD
03/98	Raymond James	Trade Reporting	17,500	NASD
03/98	Ernst & Co.	Order Entry	12,000	NASD
04/98	Piper, Jaffray	Short Sale & SOES Violations	20,897	NASD
04/98	Deutsche Morgan Grenfell	Trade Reporting	12,500	NASD
05/98	Alex Brown	Trading Violations	90,000	NYSE
05/98	J. Hancock Clearing	Books & Records	60,000	NYSE
05/98	NationsSecurities and NationsBank	Books & Records/ Inadequate Monitoring for Improper Trading/	4,000,000 (Plus 2,000,000 to NASD)	SEC
05/98	ABN Amro	Trade Violations	15,000	NASD
05/98	Everen	Trade Reporting	18,500	NASD
06/98	Troster Singer (Spear Leeds)	Trade Reporting	12,000	NASD
06/98	Fahnestock	Margin, etc.	100,000	NYSE
07/98	Dean Witter	Failure to Provide Information	10,000	NASD

Date	Firm	Violations	Penalty	Regulator
07/98	NationsBanc	Registration Failures	16,000	NASD
08/98	Cowen	Margin Failures, etc.	380,000	NYSE
08/98	Merrill Lynch	As Underwriter sold Notes Through Official Statements that Omitted Material Facts & the Risks of Investment Losses.	2,000,000	SEC
08/98	Nikko Securities	Failure to Supervise/ Inadequate Procedures/ Books & Records	2,500,000	SEC
09/98	Piper Jaffray	Order Entry Violations	12,500	NASD
09/98	Herzog Heine	Order Execution	10,000	NASD
09/98	Mayer & Schweitzer	Quotes	10,000	NASD
09/98	Bear, Stearns	Best Execution	34,584	NASD
09/98	CS First Boston	Delayed Investigation of Improper Activity by Branch Manager	500,000	SEC
10/98	Prudential Securities	Inaccurate Mark to Market in Customer Accounts, False Marketing Information Regarding CMOs	500,000	NYSE
10/98	Merrill Lynch	Order Entry	85,000	NYSE
11/98	Schroder	Regulation T Violations	25,000	NYSE
11/98	John Hancock Distribs.	Misleading Sales Material and Presentation	100,000	NASD
11/98	Paribas	Order Entry	20,000	NASD
01/99	Morgan Stanley	Order Execution	60,000	NASD
01/99	Salomon Smith Barney	Failure to Supervise/ Order Execution/ Books & Records/ Unlawful Profits & Gains	735,000 & Disgorge-ment of 24,766	SEC

Date	Firm	Violations	Penalty	Regulator
01/99	Prudential Securities	Failure to Supervise/ Books & Records/ Unlawful Profits & Gains	1,000,000	SEC
01/99	Morgan Stanley	Fictitious Quotations/ Unlawful Profits & Gains	350,000 & Disgorge-ment of 4,170	SEC
01/99	CIBC Oppenheimer	Failure to Supervise/ Fictitious Quotations/	225,000	SEC
01/99	Lehman Brothers	Fictitious Quotations/ Unlawful Profits & Gains	212,500	SEC
01/99	Bear, Stearns	Failure to Supervise	225,000	SEC
02/99	Smith Barney	Trade Execution	17,000	NASD
04/99	Hilliard Lyons	Registration	32,500	NASD
04/99	ABN Amro	Confirmations	13,500	NASD
04/99	Everen	Limit Orders	13,000	NASD
05/99	Hambrecht & Quist	Regulation T	35,000	NYSE
05/99	HSBC Securities	Books & Records, etc.	50,000	NYSE
05/99	Merrill Lynch	Order Execution	15,000	NASD
05/99	Warburg Dillon Read	Limit Orders	17,500	NASD
06/99	NationsBanc	Best Execution	15,968	NASD
07/99	Legg Mason	Confirmations	16,500	NASD
07/99	Spear Leeds	Trading	275,000	NYSE
08/99	Crowell, Weeden	Books & Records	50,000	NYSE
08/99	Everen	Order Entry	120,000	NYSE
08/99	Donaldson Lufkin & Jenrette	Trade Reporting	11,000	NASD
08/99	Tucker, Anthony	Trade Reporting	16,497	NASD

Date	**Firm**	**Violations**	**Penalty**	**Regulator**
08/99	McDonald & Co.	Best Execution	15,431	NASD
08/99	Bear, Stearns	Clearing Failures	3,500,000	SEC

APPENDIX B

THE NEW YORK TIMES, SUNDAY, AUGUST 1, 1999

GORDON GEKKO EAT YOUR HEART OUT.

Wall Street used to be about greed. Now it's about brains. About taking control of your money. So go ahead. Buy stocks. Mutual funds. Even government bonds. Online or over the phone. Want more? How about market quotes and portfolio updates. Yup. Just a mouse click away. So welcome to the world of investing. And hey. Check your cufflinks at the door.

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APPENDIX C

ETA MODEL RISK DISCLOSURE STATEMENT

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Customer Name (Please Print)

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Account Number

THE RISK OF LOSS IN ELECTRONIC DAY TRADING CAN BE SUBSTANTIAL. YOU SHOULD, THEREFORE, CAREFULLY CONSIDER WHETHER SUCH TRADING IS SUITABLE FOR YOU IN LIGHT OF YOUR CIRCUMSTANCES AND FINANCIAL RESOURCES. IN CONSIDERING WHETHER TO TRADE, YOU SHOULD BE AWARE OF THE FOLLOWING POINTS:

(1) The national securities markets are extremely efficient and competitive. Successful Electronic Day Trading typically requires skill and discipline as well as experience and knowledge of the capital markets. There is no guarantee that you will be successful in implementing your investment strategy. A substantial number of Electronic Day Traders will not be successful. Moreover, changes in market structure and competitive conditions also may affect your continued success. Only risk capital should be used for trading. Market structure and competitive changes in the markets may cause formerly successful traders to become less successful.

(2) Electronic Day Trading involves a high volume of trading activity — the number of transactions in an account may exceed 100 per day. Each trade generates a commission and the total daily commission on such a high volume of trading can be in excess of any earnings.

(3) Persons who are new to Electronic Day trading should strictly limit both the number of trades they do and the size of their trades to reduce the risk of large dollar losses during the learning process.

(4) Electronic Day Trading is designed to produce short-term profits. However, the activity also may result in losses that can exceed more than 100% of your initial capital. You are solely responsible for any losses in your account.

(5) Placing contingent orders, such as "stop-loss" or "stop-limit" orders, will not necessarily limit your losses to the intended amounts, since market conditions on the NASDAQ or any Alternative Trading System on which the order is placed may make it impossible to execute such orders. Similarly, using "market orders" can be very risky, since large gaps can occur in price movements of active stocks. You are urged in most instances to use "limit orders."

(6) Under certain market conditions, you may find it difficult or impossible to liquidate a position quickly at a reasonable price. This can occur, for example, when the market for a stock suddenly drops, or if trading is halted due to recent news events or unusual trading

activity. The more volatile a stock is, the greater the likelihood that problems may be encountered in executing a transaction.

(7) In addition to normal market risks, you may experience losses due to system failures. The firm and its clearing broker rely upon sophisticated computer software and hardware to execute transactions, which are subject to failure due to a variety of factors. In addition, NASDAQ and the Alternative Trading Systems have computer systems that often malfunction. Among other events, you may experience losses due to: system crashes during both peak and low volume periods; the loss of orders on both SOES and Select Net; and, delayed, conflicting and inaccurate confirmations on orders or cancellations that you initiate.

(8) The use of any margin or leverage in an account can work against you as well as for you. Leverage can lead to large losses as well as gains. You may sustain a total loss of the initial margin funds and any additional funds that you deposit with your broker to establish or maintain a position, and you may incur losses beyond your initial investment. If the market moves against your position, you may be called upon to deposit a substantial amount of additional margin funds, on short notice, in order to maintain your position. If you do not provide the required funds within the time required, your position may be liquidated at a loss, and you will be liable for any resulting deficit in your account.

(9) You should consult your broker concerning the nature of the protections available to safeguard funds or property deposited in your account.

ALL OF THE POINTS NOTED ABOVE APPLY TO ELECTRONIC DAY TRADING OF DOMESTIC EQUITY SECURITIES. IF YOU ARE CONTEMPLATING TRADING FUTURES OR OPTIONS CONTRACTS, YOU SHOULD BE AWARE THAT THESE INSTRUMENTS POSSESS ADDITIONAL RISKS.

THE RISK OF ELECTRONIC DAY TRADING MAY BE SUBSTANTIAL. THIS BRIEF STATEMENT CANNOT, OF COURSE, DISCLOSE ALL THE RISKS AND OTHER ASPECTS OF ELECTRONIC DAY TRADING. ONLY RISK CAPITAL SHOULD BE USED FOR SUCH TRADING.

I hereby acknowledge that I have received and understood this risk disclosure statement.

x_______________________

Signature

x_______________________

Joint Owner Signature, if any

x_______________________

Date

ELECTRONIC TRADERS ASSOCIATION
STATEMENT OF ETHICAL PRINCIPLES

Electronic Traders Association (ETA) is an association of broker-dealers that provide individuals, who day trade, with technology at a level generally available to institutions and securities dealers. ETA seeks to encourage education and awareness regarding the opportunities and risks of day trading, to promote price competition in all securities markets, and to be a resource for law, guidance and regulation in these areas.

Changes in technology now allow individuals direct access to the securities markets without the assistance of intermediaries or professional advice. These changes require day trading firms to meet high standards of ethical business conduct. As ETA members we pledge to observe these principles:

I. Responsibility to Promote Reasonable Regulation in the Interests of Our Customers and the Securities Markets

We will cooperate with lawmakers and regulators to encourage appropriate regulation to protect day traders and to make securities markets more efficient.

We are dedicated to establishing and following appropriate policies and procedures to effect full compliance with the letter and spirit of the laws and regulations which govern our activities, maintaining all appropriate state and federal licenses.

II. Responsibility to the Prospective Customer

We will be truthful in all communications with prospective customers, seeking to make sure that our communications are complete in all material respects.

We will not make misleading or exaggerated claims about our services, or the benefits of day trading, and will provide a balanced perspective in our advertisements and presentations.

We will disclose fully and candidly, orally and in writing, the risks of day trading -- knowing that successful day trading requires knowledge of the securities markets, skill, and commitment. We will not obscure the reality that most people lose money in their initial trading period and that many will not ultimately become successful day traders.

We will not make false statements, provide erroneous information, or fail to inform prospective customers of the limitations, conditions or constraints of our own systems or those of our vendors.

We will be candid in our assessment of any prospective customer's skills and potential for success. We will not open accounts for customers who do not appear to have the ability to sustain losses, or intend to trade with retirement assets, or assets necessary for daily living.

III. Responsibility to Our Customers and Our Commitment to Their Success

We will be frank and honest in our communications with customers, providing to each a statement explaining the risks of day trading, including the fact that many persons will not be successful and may lose money.

We recognize that customers' skills and potential for success will vary, and therefore we pledge to be candid in our appraisal of their individual abilities as they become apparent.

We will maintain facilities to enable customers to execute transactions efficiently -- continually developing and refining systems and vendor relationships to promote customer success.

We will uphold each customer's right to privacy and confidentiality.

IV. Responsibility to Promote Best Practices

We will promote fair and open access to the securities markets and will resist discriminatory policies and practices. We will work with lawmakers and regulators to assure fair treatment of our customers and to promote efficient markets.

We will improve continually the training we offer customers and encourage them to learn.

We will treat all persons fairly, regardless of race, religion, sex, age or national origin. We will not tolerate on our premises individuals who engage in offensive behavior.

We recognize that the markets continually change and that regulatory requirements change accordingly. We will not be satisfied with ethical standards as they were but will promote principles and practices that reflect the nature of the day trading industry as it may change.

Unanimously approved by the ETA Board of Governors, July 28, 1999.

Andover Brokerage, LLC
Mount Pleasant Brokerage Services, LP
Momentum Securities, Inc.
On-Line Investment Services, Inc.
Tradescape.Com, Inc.

The Electronic Traders Association is an association of order entry and proprietary trading firms and other vendors, affiliated companies and individuals across the United States. ETA was formed to encourage education and awareness regarding the opportunities and risks of day trading, to promote access to the NASDAQ market for all investors, to promote pricc competition in the NASDAQ market, and to promote investor fairness and confidence in the NASDAQ market.

APPENDIX E

Common Misconceptions About Day Trading

1. Day Trading is a New Phenomenon.

Day traders have existed as long as there have been markets. Specialists and market makers are given regulatory and informational advantages to day trade. However, individuals have been engaged in professional day trading on the floors of our national stock and commodity exchanges since their formation in the 18th century. Individuals have traded "upstairs" in brokerage offices at least since Edison invented the stock ticker more than 100 years ago. History shows that whenever anyone believes he has an informational edge, through proximity (being on the floor) or technology (the ticker) he trades securities for a living. What is new is that changes in technology and recent SEC regulations governing the securities markets now make it possible for on-site day traders to have virtually the same access to market information, execution and order exposure as the professionals.

2. Day Trading Firms are Entities Apart From the Rest of the Securities Industry.

Day trading firms service customers who intend to trade full time as a vocation. Trading customers have always been welcomed at brokerage firms. On-line discount firms like Schwab, E*Trade and Fidelity compete actively for active traders' business by offering them preferential technology and commission rates. Various firms share profits with their registered and unregistered traders. A clear example that day trading firms are just another part of the securities industry is seen in the Securities Industry Association's June, 1999 letter opposing the NASD's "appropriateness" proposal. In addition to speaking for SIA's membership the letter states that it reflects comments of "The Federal Regulation Committee (Chairman, the General Counsel of Prudential Securities), the Discount Brokerage Committee and committee on Technology and Regulation (Chairman, counsel of Fidelity Securities)". As noted in the text, it has been reported that larger members of the securities industry are actively seeking to purchase day trading firms, just as they have been investing in ECNs.

3. Day Traders Offer No Benefits to the Securities Markets and Investors.

Day traders provide multiple benefits to the markets and the customers who use them. Perhaps the most obvious benefits result directly from limit orders and indirectly through orders placed on ECNs. These orders foster important competition to market makers, narrowing market maker spreads (the major cost to retail investors) and providing alternatives allowing price improvement to all market participants, including institutions. An example: assume the spread on a given stock is 20-20-1/4; a day trader's limit order to buy 1,000 shares at 20-1/8, will provide an additional $125 to the proverbial Aunt Sally in Portland who is selling stock to pay for her favorite niece's freshman year at Orano. This effect is exactly what Congress had in mind in enacting the National Market System and the SEC intended in promulgating its order handling rules in 1997.

4. Day Traders Add to the Volatility of the Market.

Professor Burton Malkiel's studies show that volatility is more closely correlated with institutional ownership than day trading. But the other side of the volatility coin is liquidity. One Alternative Trading System, Optimark, claiming that day traders added approximately 100 basis points to the execution cost of a large institutional order masks such orders from public view. However, institutions, the system's intended customers, simply do not use it. Institutions understand the volatility argument is overstated; they prefer the depth and liquidity of the market, the increasing quote competition and enhanced price discovery mechanism which are strengthened by day traders. As Professor Samuelson in his classic textbook on economics wrote regarding day traders (circa 1955) "Traders make the market less thin. Because of them, any investor can liquidate his market holdings at any time at some price... liquidity enhances the attractiveness of securities..." In fact, to service day traders various ECNs - unlike Exchange specialists and market makers - now make available their entire book of orders. Thus the average customer can see all the prices. As one fund manager wrote recently in the New York Times: "The Internet takes out the middlemen who are not creating value. John Q. Investor should care because if he wants to get a maximum return on his investment dollar, he does not want to pay anyone any more than he has to." Day traders are a key instrument for pre and post transparency. (Providing meaningful pricing data for all investors and transparency reduces "gaming" by market makers, especially at the opening of trading.

5. Day Traders are Not Informed of the Risks of Day Trading.

ETA not only supports the NASD's risk disclosure proposal, ETA believes it does not go far enough. ETA members already require that prospective customers sign a statement containing risk disclosures significantly beyond what the NASD proposes. But disclosure or not it is simply impossible for on-site day traders not to be aware of their trading risks. In a typical on-site office the traders are in close proximity to each other, if they have been trained at the firm they will have seen numerous examples of failed trades and strategies. In simple terms, no day trader could possibly be unaware of these risks. If as one blue sky commissioner's reported, 67 of 68 day traders in an office lost money, traders would be fleeing the office screaming "plague". More particularly, for those who do lose money the understanding and acceptance of the risks, and their own market decisions, explains why the NASAA Report cited no customer complaints. In fact, the Atlanta Constitution reported in August that the director of the Massachusetts Securities Division admitted that the Division's investigations did not stem from customer complaints.

6. Seven, Eight or Nine Out of Ten Day Traders Lose (All) of Their Money.

The keystone of the attempted demonization of day trading firms by the NASAA Report is its claim that a high percentage of day traders lose money. When offered the opportunity by ETA to conduct an impartial study of the subject NASAA refused. When the NASAA Report was released the numbers provided by its "expert" were notably incredible: 17, the number of accounts sampled, was small; the accounts came from one office of one non-ETA firm; the sampling was of two year old account information; the period focused on covered four months;

the percentage of alleged losers had dropped from previous references of 8 or 9 out of 10 to 65%; and, most bogus of all, the standard for testing was not, as one would expect, traders who had lost all of their money, but traders who if they continued trading would realize a "Risk of Ruin", that is, against all common sense they were destined at some point in the future to lose all their money. ETA has determined to put these fantasy figures to rest. It expects to commission KPMG to do a study based on thousands of day trading accounts, over a considerable period of time at a number of firms. ETA believes that study will bear out its members' estimates of day trading profitability; that is, approximately 60% of day traders lose money in their three to five month learning period, thereafter well over 60% make money, averaging $25,000 or more in monthly profits, while the balance lose $6,000 - $8,000 monthly.

7. Day Traders are at a Trading Disadvantage to Market "Professionals".

The technology platforms utilized by day traders are the state of the trading art. That they are beyond the existing technology at many firms was reported in an August 13, 1999 New York Times article, which wrote that Fidelity Investments, Lehman Brothers and Instinet are considering "adopting the software platforms of day trading firms..."

One institutional trader has stated: "Individual traders now have a lot of the same tools we institutions do; real-time quotes, push button executions..." Five months of training and experience puts customers at the same level of market knowledge skills as the traders at market making desks. In fact, the knowledge level of the day traders may be higher given the advanced level of education of day traders compared to traders employed by market makers. Market makers recognize that there is at least a level playing field in skills and technology. To quote the President of a major market maker, "The genie is out of the bottle and it ain't going back in."

8. Day Traders Routinely Violate Securities Regulations.

Forgery, false advertising, evasion of margin regulations, improperly executing short sales, promoting unregistered investment advisors, are the most sensational charges leveled by the NASAA task force against day trading firms. But, as the NASAA Report shows, neither the SEC nor NYSE has ever brought a case aimed at day trading practices, while the NASD, which annually examines all day trading firms, has fined one firm $25,000 for failure to register certain employees (and another $7,500 for order entry violations). And this is in a period in which the SEC, NYSE and NASD have brought numerous actions against household name brokerage firms for infractions of the myriad securities regulations. Thus in August alone the NYSE and NASD disciplined such firms as Everen Securities, McDonald Investments, Inc., Donaldson Lufkin and Jenrette and Tucker, Anthony, Inc. In fact, other than Massachusetts, which wrote the NASAA Report and is the home of its chairman, only a handful of states have taken action. These have brought in all four cases for failures to file broker-dealer reports or register; one state, apparently finding no securities law violations, claimed the firm involved had violated the state's franchise law. That the NASAA effort is in reality driven by one state is put in further context by the fact that the nation's five most populous states, California, New York, Illinois, Florida and Pennsylvania have taken no action. Day trading is used by the NASAA leadership to promote its position in the regulatory world. As NASAA President Hildredth stated "to reposition ourselves... with a little imagination we can find [the news media] stories to write about". It is clear that most regulators do not agree that a customer's authorization (in writing) of a firm employee to sign the customer's name when he is unavailable to sign is "forgery", or that one customer's trading his parents' money amounts to his being an unregistered investment advisor; or that there have been violations of short sale regulations. As a matter of fact even the NASAA Report admits that the states have no regulatory role in securities credit matters. Thus what the NASAA Report pumps up beyond all recognition are brokerages' common failings regarding books and records, sales practices and order entry and execution.

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EXPERIENCE:

CONSULTANT (FUTURES & SECURITIES) 1986- PRESENT

Provide investment analyses, damage calculations; and consulting services for securities and commodity disputes. Special expertise in options and commodities. Knowledgeable in all aspects of these markets including theory, practice, compliance and suitability. Expert in trading risk assessment and statistical expectations. Insightful analyses based on professional trading experience, advanced analytical background, and quantitative analyses techniques.

Consulted with numerous law firms, individuals, and the State of Florida. Represented clients in California, Michigan, Ohio, Louisiana, Florida, Virginia, Pennsylvania, and Massachusetts. Provided expert testimony in Federal Court, State Court, CFTC Reparations, and arbitration proceedings of the National Association of Securities Dealers, National Futures Association, American Arbitration Association, and New York Stock Exchange.

PUBLISHER, COMMODITY TRADING SERVICE *1985-1986*

Edited and published "TRADING POINTS," a national futures trading service. Published daily hot line trading recommendations and biweekly reports on index futures and options markets based on proprietary computer models and indicators developed as a professional trader.

PROFESSIONAL TRADER *1982-1985*

Traded managed option and futures accounts for suitable clients. Developed new technical trading indicators and trading systems based on market research and quantitative, analytical background. Honed trading skills in professional trading contests.

INVESTMENT ADVISOR *1978-1985*

Edited and published the "ROI ADVISOR," an investment letter on the stock, bond, and gold markets. Developed low price stock strategy that returned over 30% per annum during this period. Developed client base through referrals. Served as investment consultant to individuals, trusts, and pension funds.