

April 9, 2004

**TESTIMONY OF SCOTT DESANO
ON BEHALF OF FIDELITY MANAGEMENT AND RESEARCH COMPANY
AT HEARINGS BEFORE THE SECURITIES AND EXCHANGE COMMISSION
ON PROPOSED REGULATION NMS**

File No. S7-10-04

April 21, 2004

Good morning. My name is Scott DeSano. I head the Equity Trading Desk at Fidelity Management and Research Company. As of March 31, 2004, Fidelity acted as the investment manager of over 200 equity mutual funds registered under the Investment Company Act of 1940, representing aggregate equity assets of over \$575 billion. As a fiduciary for the Fidelity Funds, we are an active and substantial participant in the secondary equity trading markets in this country. Our funds have a vital interest in efficient, transparent, reliable and fair trading markets -- markets where order flow is earned through innovation, service and competition.

With decimalization, and the dramatic growth of electronic trading systems and alternative market centers, the Commission's proposals come at a crucial stage in the evolution of our equity trading markets. Given the importance that we attach to the role of

open and free competition in shaping our nation's equity markets, we commend the Commission for including in proposed Regulation NMS a provision that will afford informed investors the freedom to opt-out of the trade-through rule. The flexibility conferred by the opt-out provision is crucial to an investment manager such as Fidelity because it will preserve our ability to perform our fiduciary duty to its fullest extent. That duty is to use our independent judgment solely in pursuit of the best executions available to the mutual funds under our management. To carry out our fiduciary responsibility, it is essential that we retain the ability to exercise our judgment in deciding how to size the orders we present for execution, how much pricing and timing discretion to give the brokers that serve our funds, and whether to give those brokers the power to seek liquidity without regard to the trade-through rule.

We understand that market centers with a vested interest in preserving their market share of trading volume may contend that support for an opt-out provision is antithetical to the goal of best execution. The argument is that by supporting a rule that allows us to choose among competing market centers, we somehow favor speed or certainty of execution *at the expense of best price*. We categorically reject this contention. Speaking

for Fidelity, let me make one thing clear: In seeking best execution in trades for our funds we have one objective — and only one objective — in mind. That objective is to obtain the best overall price for our funds' trades. We view speed and certainty of execution as means to an end, and that end is overall best price.

Experience has taught us a very clear lesson. Given the dynamics of our trading markets and the rapid and sudden shifts in stock prices, the overall best price for the purchase or sale of stocks for our funds often depends upon our ability to lock in a price at a given moment for all or a significant part of our trade. If we are compelled, against our better judgment, to break up our orders and execute them over an extended period of time, in many cases this will lead to inferior all-in prices for our funds. An opt-out provision to the trade-through rule will not subordinate best price to certainty or speed of execution. We value certainty and speed of execution precisely because these factors play an indispensable role in obtaining best price for our funds' trades.

To serve our fund investors who have entrusted their money to us, we and the brokers we employ need to have the full range of discretion in executing orders. We,

as is true for all other fiduciaries, should not be constrained by a trade-through rule which would compel, without exception, that we walk the market up or down for every stock our funds wish to purchase or sell when, at least in certain instances (especially in rapidly shifting markets experiencing sharply fluctuating levels of liquidity), fiduciary judgment tells us that such a course would be unwise and would disadvantage our funds.

Those who oppose the flexibility of an opt-out provision for fiduciaries contend that the ability of mutual funds and other institutional investors to obtain best execution should be curtailed in the name of fairness to third parties in the marketplace, especially retail investors, even when this will result in an inferior overall price for mutual funds and other institutional investors. Our answer is that institutional investors should be allowed to do what is best for the investors on whose behalf they act as fiduciaries, without having to provide a subsidy to others. If the markets are left open and free to compete based upon innovation and service, rather than based upon government-imposed order routing rules, the efficiencies and economic self-interest of investors, large and small, will naturally lead to the evolution of a national market system that will redound to the benefit of all market participants.

We understand that a more limited argument against an opt-out provision holds that a truly “fast” market should not be traded through by another fast market. We believe it is unwise, as a matter of public policy, for the Commission to condition the flexibility afforded by an opt-out provision under current circumstances, even when a market is presumed, for regulatory purposes, to be “fast.”

First, a market deemed “fast” at a point in time coinciding with a Commission rule may not be “fast” in the future and, in any event, may not always be “fast” when the time it takes to route orders to and from the market via existing linkages is taken into account. If a market can instantaneously (i) respond to an order at the time of order entry and (ii) confirm an execution or re-route the order (or a portion thereof) to another market center in another microsecond to the market showing the next best price, perhaps this would satisfactorily address the issue of speed. It is not today’s reality, however.

Perhaps the more important reason to preserve opt-out flexibility even among fast markets is that fiduciary duty and economic self-interest of market participants

counsel against the need for government-imposed trading rules. At the least, the Commission should give the market an opportunity to operate without the constraints of inter-market order routing requirements before imposing a rigid trade-through rule applicable to all market participants under all circumstances. If there really is no incentive to avoid fast markets or to select among them, a rule is not needed to require an institutional investor, or a broker acting on its behalf, to act in its economic self-interest.

At Fidelity, achieving the best possible performance for our funds' investors is the overarching goal. We continually seek to evaluate all aspects of our operations, from research and stock picking, to order generation and execution. We are not satisfied with "good enough" in executing trades — good enough is not our objective for our fund shareholders. We seek to beat the average execution and we charge our brokers with the responsibility to do all they can to deliver that result. For that reason, we wish to have maximum flexibility in making order-routing decisions and not to be fettered by order routing rules that will prevent us from doing our utmost for our investors.

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We appreciate the opportunity to give our comments to the Commission on these important matters. We hope our views will be helpful to the Commission and its staff as they continue to weigh these issues. I would be pleased to answer any questions you may have.