

# PARK AVENUE *Securities*

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April 12, 2004

Mr. Jonathan G. Katz  
Secretary  
U.S. Securities and Exchange Commission  
450 Fifth Street, N.W.  
Washington, D.C. 20549-0609

Re: File Number S7-06-04  
Release Nos. 33-8358; 34-49148; IC-26341  
Proposed Amendments to Rules 15c-2-2 and 15c2-3  
Under the Securities Exchange Act of 1934

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Dear Mr. Katz:

Park Avenue Securities LLC ("PAS")<sup>1</sup> appreciates the opportunity to provide the U.S. Securities and Exchange Commission ("Commission") with comments on Release No. 33-8358; 34-49148; IC-26341 by which the Commission proposes to create Rules 15c-2-2 (confirmation disclosures) and 15c2-3 (point-of-sale disclosures) under the Securities Exchange Act of 1934.

PAS supports the general idea of additional disclosures to customers to assist them with their investment decisions; nonetheless, the proposed rules present multiple concerns to PAS as well as to other broker-dealers. To this end, PAS has participated in numerous communications with various industry groups, such as the Securities Industry Association (SIA), the Investment Company Institute (ICI), the American Council of Life Insurers (ACLI) and the Financial Services Institute (FSI), among others, and anticipates that these groups will submit comment letters to address issues that have commonly raised concerns for all broker-dealers. Accordingly, our letter to the Commission will attempt to address several issues specific to PAS's business model, a business model that we believe is shared by a number of other broker-dealers.

PAS respectfully differs from the Commission's apparent view that all broker-dealers are alike and structured similarly so that the proposed rules can be implemented uniformly across over 5,000 firms, including non-wirehouse, non-fund supermarket business models. PAS favors disclosures that are clear, meaningful and understandable to customers and that are presented by the right party. However, as we discuss below, PAS's direct subscription mutual fund business does not easily lend itself to a straightforward implementation of the proposed rules.

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<sup>1</sup> Since commencing operations in May 1999, PAS has been a broker-dealer registered under the Securities Exchange Act of 1934 (BD# 46173) and a member firm of the NASD. PAS is directly owned by The Guardian Insurance & Annuity Company, Inc. ("GIAC") and indirectly owned by The Guardian Life Insurance Company of America, a New York mutual insurer ("Guardian"). PAS serves as Guardian's "retail" broker-dealer and primarily offers mutual funds and variable insurance products through Guardian's General Agency distribution system. Guardian's 85 General Agencies comprise approximately 3,200 career force insurance agents of whom approximately 2,800 are Registered Representatives of PAS. On the brokerage platform, PAS maintains a fully disclosed clearing relationship through National Financial Services LLC ("NFS LLC").

## **DIRECT SUBSCRIPTION BUSINESS**

By the phrase “direct subscription mutual fund business”, we mean the check-and-application business processed through a broker-dealer in a non-brokerage account where customer assets are held at the fund company.<sup>2</sup> In this type of business, customers may utilize the services of a Registered Representative initially to establish an account with a mutual fund family, but customers typically will engage in subsequent transactions (*i.e.*, deposits, sales, exchanges or redemptions) directly with the mutual fund sponsor, bypassing the Registered Representative and the broker-dealer.

In direct subscription business, the mutual fund sponsor receives checks for additional deposits made payable to the fund directly from customers, deposits all checks into the customer’s account held at the fund, executes all trades, accepts exchange and redemption requests directly from customers, and generates and sends all statements and confirmations. While the broker-dealer is identified as the dealer of record, the broker-dealer may not be involved in account transactions depending on the way in which the customer chooses to engage in fund transactions. To the extent the customer engages in transactions directly with the fund company, PAS will receive any applicable compensation as the dealer of record, but may not have prior knowledge of the specific transactions that generate that compensation.

For PAS, direct subscription business comprises over 55% of our mutual fund business, accounting for a substantial dollar amount of revenue last year. PAS offers more than 80 different fund complexes to serve the needs of our non-brokerage clients. In 2003, PAS non-brokerage customers effected the majority of their transactions directly with mutual fund sponsors, *i.e.*, more than one million purchases. In these cases, PAS becomes aware that trades occurred when it receives copies of the confirmations from each mutual fund sponsor and receives fund sponsor compensation in accordance with a scheduled commission payment schedule. Because of the nature of direct subscription business as described, PAS and other broker-dealers who engage in direct subscription business are not positioned to carry out the Commission’s proposed amendments regarding point-of-sale disclosures and confirmations. Should the rule proposals be enacted as described, PAS would incur considerable costs to implement the rules, far in excess of the Commission’s estimates.

### **A. POINT OF SALE DISCLOSURES**

#### **1. REQUIRED DISCLOSURES ARE MORE PROPERLY MADE BY FUNDS IN PROSPECTUS**

PAS respectfully disagrees with the Commission on its position that it is the broker-dealer’s responsibility to disclose the information being required by the proposed rules related to distribution costs.

It is the fund complex that controls distribution costs. It is the fund complex that knows the numerous ways that these costs are incurred. It is the fund complex that knows its arrangements with the various selling broker-dealers. Accordingly, it is the fund complex that is in the best position to make the disclosures contemplated by the Commission in the rule proposals.

To require broker-dealers to make such disclosures and bear all costs of implementation, the Commission is inappropriately attempting to transfer this burden that aptly belongs to the fund complexes to broker-dealers as well as impractically expecting uniformity among over 5,000 broker-dealers to interpret a fund’s data in a consistent manner.<sup>3</sup> As aforementioned, PAS offers its clients over 80 fund complexes in the direct subscription business and hundreds of mutual funds through its brokerage platform. There will

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<sup>2</sup> The business model for variable products is conducted on a direct subscription basis as well.

<sup>3</sup> For example, if broker-dealers were required to disclose distribution costs and fund complexes were not required to provide the data, then PAS would need to review manually every prospectus annually to identify the appropriate costs per share class and build a system to calculate costs for both a \$10,000 model and individual transactions. PAS has contacted a vendor that would maintain a database of sales charge/12b1 fee information for \$200 per CUSIP annually. For PAS’s direct subscription business, there are approximately 3,900 CUSIPS involved; on the brokerage platform, PAS offers the universe of mutual funds made available through NFS LLC, which consists of several thousand CUSIPS. From simply the perspective of data retention, the costs may exceed one million dollars annually.

be substantial drains on resources and manpower associated with the gathering, compiling, updating and communication of the proposed disclosures. Invariably, these significantly higher costs to be borne by the broker-dealers, in turn, must be passed onto customers.

Furthermore, as observed in the NASD's Mutual Fund Breakpoint Refund directive, many non-wirehouse broker-dealers that engage in direct subscription business needed fund sponsors to provide additional information in order to contact customers and analyze transactions. Broker-dealers would be hard-pressed to comply with the disclosure requirements contemplated by the Commission in the rule proposals without corresponding mandates to the mutual funds to assist in this process and to provide additional information in a meaningful manner.

PAS respectfully recommends that the Commission consider proposals to enhance the disclosures made in the prospectus with respect to distribution costs and conflicts of interest without requiring broker-dealers to replicate information unnecessarily through additional disclosure obligations.

The prospectus issued by a fund complex constitutes the proper disclosure document. By requiring other documents to synthesize, highlight or abridge the information found in a prospectus, the rule proposals may have the unintended effect of diluting the importance of the prospectus. A customer's overall decision-making process includes more than just a review of costs and conflicts.

Should the Commission determine that a more focused presentation of the proposed point-of-sale disclosures would be most beneficial and apropos in the prospectus, PAS suggests that the Commission may require broker-dealers to disclose conflicts of interest in a separate document to clients in two versions: (1) a disclosure where there are no revenue sharing arrangements beyond the standard sales charge and 12b1 administrative fees paid to the broker-dealer and (2) a confirmation disclosing existing revenue sharing arrangements beyond the standard sales charge and 12b1 administrative fees paid to the broker-dealer.

## **2. POINT OF SALE DISCLOSURES**

We respectfully request that the Commission consider adding another exception to proposed Rule 15c2-3(e) that addresses direct subscription business. As defined by the Commission, "point-of-sale" generally occurs "immediately prior to the time that the broker, dealer or municipal securities dealer accepts the order from the customer." At point-of-sale, broker-dealers will be required to provide a disclosure document that includes information directly related to the particular transaction at hand.

The applicability of proposed rule 15c2-3 with respect to point-of-sale disclosures in the context of direct subscription business is unduly burdensome. Because of the nature of direct subscription business, the point-of-sale moment may be difficult to pinpoint and the "indications of interest" concept may be difficult to implement, since PAS has no control over the receipt of certain transactions and is in no position to "hold" a transaction. There is no window of opportunity for PAS to provide point-of-sale disclosures. PAS respectfully requests that the Commission give serious consideration to revising this requirement.

In addition, PAS, as an introducing broker-dealer that claims exemptions under Securities Exchange Act Rule 15c3-3(k)(2)(i) and (ii), must promptly transmit all funds received in connection with its securities activities to its clearing firm. These proposed rules would seem to pose conflicts to this regulatory requirement.

## **B. CONFIRMATIONS**

Currently, in addition to investment companies relying on the applicability of two no-action letters under Rule 10b-10, broker-dealers also rely on the relief found in these no-action letters that allow the fund sponsor to send confirmations to clients in direct subscription business. Any rescission of the relief will create significant additional burdens on the broker-dealer and cannot be properly implemented without new requirements on mutual funds to provide necessary information to broker-dealers.

In the direct subscription business, PAS believes that a second confirmation from the broker-dealer that merely repeats the information seen on the confirmation sent by the fund sponsor provides no added value to the client. In fact, it would seem pointlessly duplicative, would have had no bearing on assisting the client to make an informed investment decision, and thus is unwarranted considering the costs incurred. That being the case, there is no justification for the added expense to the broker-dealer to produce and mail this duplicate confirmation.

PAS respectfully requests that the Commission reconsider the disclosures warranted for confirmations, particularly in the context of direct subscription business and other pending rule proposals from the Commission.

**C. EXTREMELY HIGH COSTS**

PAS respectfully disagrees with the Commission's projected costs to carry out these proposed amendments. PAS estimates that the production expenses will be \$1-2 million dollars annually (excluding any programming costs or systems development) to address the mailing of confirmations on the direct subscription business.

**D. INAPPLICABLE TO VARIABLE PRODUCTS**

PAS strongly disagrees with the Commission as to the applicability of the proposed rules for variable products. The proposed rules appear predicated on a mutual funds model and do not fit variable products well, if at all. As variable products are not structured like mutual funds, the proposed disclosures do not translate easily into definable terms or concepts related to variable products, *e.g.*, asset-based charges and service fees, trail compensation, issuers, fund complex, revenue sharing, portfolio securities transactions, comparison ranges, multiple broker-dealer commissions, concession, timing issues related to purchases and reallocations, among others. As we do not understand how the proposed rules could be implemented in the variable products context, PAS refrains from commenting further on this issue at this time and requests clarification from the Commission.

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Given the substantial financial and organizational burdens that the proposed rules would impose on firms such as PAS, we respectfully request that the Commission re-examine the current proposal, taking into consideration the points raised in this comment letter and those of industry groups.

Sincerely,  
Joanne B. Mack  
President  
Park Avenue Securities LLC