



A N E W Y O R K L I F E C O M P A N Y

April 13, 2004

By email to rule-comments@sec.gov

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

Re: File No. S7-06-04

NYLIFE Securities Inc.¹ (“NYLIFE”) welcomes the opportunity to provide the U.S. Securities and Exchange Commission (“Commission”) with comments in response to the Proposed Rules and rule amendments under the Securities Exchange Act of 1934 as set forth in File No. S7-06-04.² Under the Proposed Rules, the Commission seeks to require broker-dealers to provide purchasers of mutual funds, variable insurance products, and Section 529 plan securities with particular items of information at the point of sale and in transaction confirmations. Our comments are limited to aspects of Proposed Rules 15c2-2 and 15c2-3, and will not specifically cover suggested changes to Rule 10b-10 or Form N-1A.

NYLIFE strongly supports the Commission’s objectives of improving the quality of disclosure of product features and costs and enhancing investor protection. It is axiomatic that customers are best served by having access to all material information so that they may make informed investment decisions. Our concerns principally involve the manner in which important disclosure is delivered to customers (whether orally, by prospectus, in confirmations, and/or so-called point-of-sale documents). NYLIFE shares what is surely the goal of the Commission to ensure that all appropriate and required disclosures are conveyed to customers in the most clear, comprehensible, and cost-efficient manner possible.

General comments on 15c2-2 and 15c2-3

With the introduction of Proposed Rule 15c2-2, the Commission signals its intention to move away from its historical position that a broker-dealer may satisfy its mutual fund³ confirmation disclosure obligations without providing a transaction-specific document that discloses information about sales loads and third-party remuneration, on

the condition that the investor receives a fund prospectus containing adequate disclosure at or before completion of the transaction. Given the highly significant new expenses that would attend the enactment of the Proposed Rules, as acknowledged by the Commission in the Release, as well as the potential availability of much less expensive but equally effective means of disclosure, we suggest that further consideration be given to reasonable alternatives. We do not believe that a clear case has been made that establishing a confirmation requirement with the specific elements set forth in Rule 15c2-2, or mandating the point-of-sale disclosure contemplated by Rule 15c2-3, would materially advance the cause of investor protection in a way that could not also be accomplished by modifying prospectus disclosure requirements.

We take no issue with the providing the investing public with more specific disclosure concerning the areas identified in Rules 15c2-2 and 15c2-3. Instead, we suggest that the Commission's aims would be as achievable by further refining its recent efforts to make mutual fund prospectuses more readable and user-friendly, as it would by creating the onerous burdens of requiring firms to deliver confirmations and point-of-sale disclosure documents that comply with the Proposed Rules. Certainly the financial impact on the industry and individual firms would be dramatically less significant than is currently forecasted if the required disclosure were made through changes in prospectus forms rather than transaction confirmations and newly-mandatory point-of-sale disclosure documents.

The Commission estimates that complying with Rule 15c2-2 will require initial industry costs of \$850 million and ongoing annual costs of \$1.99 billion, and that complying with Rule 15c2-3 will require initial costs of \$450 million and ongoing annual costs of \$975 million. In order to justify the anticipated burden on the industry, as well as the estimated costs to individual firms (nearly \$550,000 per broker-dealer), we submit that the regulatory case in favor of the rules' enactment must be overwhelming. Unless the Commission is completely satisfied, based on an exhaustive consideration of all practical alternatives, that no amount or type of prospectus disclosure could serve as an adequate substitute for the methods of disclosure mandated by the Proposed Rules, we urge that this matter be delayed pending further study so that less burdensome alternatives may be explored.

For nearly three decades, the Commission has not required transaction-specific disclosure on confirmations regarding fees associated with mutual fund transactions, where information enabling an investor to calculate such fees is included in the product prospectus delivered to the customer. In 1977, in the adopting release for Rule 10b-10,⁴ the Commission established the proposition that if information required by Rule 10b-10 were contained in the relevant fund prospectus, the broker-dealer would not be required to repeat the information on transaction confirmations. In 1979, SEC staff advised the Investment Company Institute ("ICI") in a no-action letter (the "1979 letter") that certain fees associated with mutual fund transactions did not have to be disclosed on transaction confirmations as long as the requisite fee information was included in a prospectus that

“disclosed the precise amount of the sales load or other charges or a formula that would enable the customer to calculate the precise amount of those fees.”⁵ In 1994, the Staff advised in another no-action letter to the ICI (the “1994 letter”) that non-disclosure of mutual fund commissions on confirmations was inappropriate, and that it intended to withdraw the 1979 letter.⁶ Notwithstanding the 1994 letter, the Commission seemed to confirm the underlying principle of the 1979 letter in February 2000 in an *amicus curiae* brief in Press v. Quick & Reilly (U.S.D.C., S.D.N.Y), where it stated that “as a general principle delivery of a prospectus containing sufficient disclosure can satisfy a broker-dealer’s obligations under Rule 10b-10.” In the current Release, the Commission acknowledges that as a result of discussions between the mutual fund industry and SEC Staff following the 1994 letter, and an apparently mutual recognition that disclosing transaction charges through prospectus fee tables tended to be more accurate than estimating charges on confirmations, the Staff resolved not to withdraw the 1979 letter. Notwithstanding that somewhat circuitous history, the Commission announces in the current Release its intention to withdraw the 1979 letter after all.

In view of the SEC Staff’s repeated longstanding affirmation that in the mutual fund context, prospectus disclosure can serve as an adequate (and in terms of accuracy, superior) substitute for confirmation disclosure, and, given the enormous costs projected to accompany enactment of 15c2-2, the question arises whether present circumstances justify the pending change in policy and direction. The Release attempts to address this subject by referring to the tremendous growth of the mutual fund industry since 1977, the extent to which Americans rely on mutual funds for their retirement, the increase in mutual fund assets and the sheer number of mutual funds on the market, the growth in the number of funds that are affiliated with broker-dealers, and other changes. While those facts are indisputable, the obviousness of the remedy – especially one that will be so costly -- is less so. It is not clear from the Release exactly what study has been undertaken to justify the conclusion that only by establishing rules on the scope of 15c2-2 and 15c2-3 can the interests of investors be adequately protected. We recognize the recommendation of the Joint NASD/Industry Task Force on Breakpoints that mutual fund confirmations include front-end sales load disclosure, yet that recommendation alone could surely be accommodated without the Commission simultaneously adopting the other extensive changes contemplated by the Proposed Rules.

Given the expected burdens on the securities industry that would accompany the enactment of 15c2-2, we respectfully request that the Commission closely scrutinize whether it is now appropriate to abandon the principle that adequate prospectus disclosure offers sufficient customer protection. It is not clear from the Release whether due consideration has been given to a more comprehensive review of Forms N-1A and N-4, for example, with a view towards further simplifying product prospectuses – while also bolstering existing prospectus requirements - to ensure that customers have ready access to all material information. We would also submit that enhanced prospectus disclosure would obviate the “point-of-sale” document contemplated by Proposed Rule 15c2-3.

Specifically, Form N-1A currently requires disclosure of the expenses applicable to a hypothetical \$10,000 investment in each class of fund shares offered after one, three, five and ten years. As an alternative to providing transaction-specific disclosure on the confirmation and at point-of-sale, the current requirement could be expanded to include expense and compensation information for each share class and at each breakpoint level offered by the fund. Such information would be depicted at the end of each year for which a contingent deferred sales charge would be applicable, as well as after ten years. While perhaps not providing the precision contemplated by the Proposed Rules, such disclosure would provide the prospective investor with a fair estimate of the comparative fees and payments associated with the contemplated investment. In addition, to ensure that investors are apprised of potential conflicts or special compensation, firms could be required to furnish a point-of-sale document with pertinent disclosure, as suggested in the draft point-of-sale document that accompanied the Release. This approach would enable firms to avoid a substantial part of the costs attendant to providing the transaction-specific disclosures contemplated by the Rules and is consistent with the objective that the Commission seeks to achieve.

The alternative discussed immediately above provides much more complete disclosure than Proposed Rule 15c2-3 would permit. That is, when the value of a proposed purchase is not reasonably estimable, Proposed Rule 15c2-3(a)(1) would permit a broker-dealer to satisfy its disclosure obligations by depicting the required information with respect to a proposed \$10,000 investment. Our proposal would result in an investor's being able to compare costs at each breakpoint level offered. To ensure that the investor has read and had an opportunity to ask questions about the comparative disclosure, broker-dealers could also be required to obtain a separate written acknowledgement to that effect on a form that includes the required disclosure. As an added protection, Rule 17a-3 then could be amended to require that a copy of the signed acknowledgement be sent to the investor within 30 days of the account's opening.

If registered representatives are required to deliver transaction-specific point-of-sale disclosure, broker-dealers may find themselves compelled to automate the delivery of the required information. Absent automation, errors in manual computation of the required disclosures could expose firms and their registered representatives to potential civil liability. Automation of this process would surely be costly, both for initial design and programming, as well as for updating systems to reflect changes in fees, expenses or compensation programs. The expenses associated with obtaining information from myriad fund companies and performing the programming necessary to update all computers that are used to generate the required disclosure forms could very well cause firms to limit their mutual fund offerings to those fund complexes whose compensation is generous enough to cover the additional expenses and provide a reasonable profit. Thus, the indirect consequences of the Proposed Rules could be to limit investors' investment choices and increase expenses paid by the investing public, two undesirable results. The enhanced prospectus disclosure provision that we suggest above would place the burden of providing the required disclosure on the fund company, which is in the best position to

know its expenses and compensation programs. Changes to required disclosure would need to be made only one time and in one place – the prospectus – at a considerably lower cost to the entire securities industry.

Beyond the foregoing, our concern with Proposed Rule 15c2-3 is a practical one. When an associated person delivers the point-of-sale document to a customer together with a copy of the product prospectus, there may be a temptation on the part of the recipient to read and review the relatively brief point-of-sale document rather than the inherently longer product prospectus. Given the rationale underlying the Proposed Rule of building and bettering investor awareness, we are concerned that introducing the point-of-sale document into the disclosure process may be at the risk of a fair percentage of customers surmising that a review of the prospectus is unimportant or, worse, unnecessary. Such a result would clearly and obviously be inconsistent with the thrust and spirit of the Proposed Rule. Thus, the Commission should recognize that as a practical matter, providing an investor with an additional point-of-sale disclosure that is different from what is set forth in the prospectus at the point of sale may in the end prove counterproductive. While certainly firms can and would train their associated persons to explain the respective purposes of the point-of-sale document and the prospectus to customers, it is undeniably the case that the typical contemporary investor has a limited amount of time to devote to investment research. In short, we are concerned that enactment of 15c2-3 may undermine its own rationale of improving investor awareness.

In our view the Commission's current position, perhaps with modifications along the lines of those suggested herein, continues to represent a reasonable and workable approach to customer protection in the area of mutual fund disclosure. The potential disclosure requirements contained in 15c2-2 and 15c2-3 would represent major modifications of longstanding Commission policy. Should the rules be enacted in forms roughly equivalent to what are set forth in the Release, firms will (as the Commission acknowledges) face significant resource challenges in the form of software reprogramming, systems updating, upgrading and reprogramming printing systems, and printing and postage costs. We respectfully submit that the case has yet to be made whether on a net basis the contemplated dramatically-increased costs are justified by the uncertain prospect of a better-informed investing public, relative to other means of delivering the disclosure. As stated above, while we recognize that the enhanced disclosure proposed in Proposed Rules 15c2-2 and 15c2-3 would inure to the benefit of the investor, and while we submit no objection to the proposed elements of the enhanced disclosure, it is by no means clear that conveying transaction-specific disclosure in the manner proposed is the only means to accomplish the Commission's objective.

Comments on impact of Proposed Rules on variable insurance products

The above comments apply equally to variable insurance product sales. We would also take this opportunity to raise the following issues specifically with respect to their application to variable products:

(i) We note in the discussion of Proposed Rule 15c2-2 the issue as to whether firms should be permitted to use a single confirmation for transactions in both the variable product itself and the underlying funds. We see little basis for mandating that separate confirmations accompany a customer's selection of investments in underlying funds within the context of a variable insurance product. Variable insurance and annuity investors receive copies of relevant fund prospectuses for both product and its underlying funds that disclose all matters required under Commission rules. Upon issuance of the policy, the policy itself and a confirmation reflecting the investments chosen to fund –the policy are delivered to the investor. Unlike mutual funds, variable insurance products are subject to regulation under state insurance laws, which give the investor the right, under so-called “free-look” provisions” (which range from a minimum of ten days to even greater periods), to return their policies within a specified time period and receive a refund of premiums. Similar rights are granted to investors under many state insurance replacement regulations. Under New York Insurance Regulation 60, for example, investors have up to 60 days to return a policy purchased in a replacement transaction and receive a full refund.

(ii) Proposed Rule 15c2-2 contains terminology that appears applicable only to mutual funds. Given the pricing and structure of variable insurance products, disclosure regarding alternative share classes, front-end loads and breakpoints would typically be inapplicable.

(iii) We request clarification of the disclosure required for variable insurance products containing multiple sub-accounts that invest in underlying funds which have 12b-1 fees. Does each sub-account investing in an underlying fund that charges a 12b-1 fee need to be listed separately? Must the firm specify the corresponding 12b-1 fee amount for each underlying fund?

(iv) Under Proposed Rule 15c2-2, would payments by life insurers of ongoing asset-based trail commissions to selling firms in relation to variable product sales be considered “asset based sales charges?” Unlike 12b-1 fees, such payments are not required to be disclosed in the fee table as sales charges. Such fees are not deducted from separate account assets and have no analogue in the mutual fund industry.

Given the differences between variable products and mutual funds, we respectfully request that the Commission consider the unique features of variable products with a view towards exempting them from the requirements of Proposed Rules 15c2-2 and 15c2-3. If additional regulation is deemed necessary, we respectfully submit that separate provisions for variable insurance products, which are specifically tailored to their characteristics, may be more appropriate and will be subject to clearer interpretation by the insurance industry.

Conclusion

To the extent that the Commission sees fit to enact Final Rules on the order of what are being currently proposed, we respectfully request that the Commission allow lead time of at least eighteen to twenty-four months so that firms can adequately plan and execute their strategies for compliance.

We appreciate this opportunity to express our concerns about these very important proposals, which have such potentially far-reaching consequences for our Company and for the industry at large

Sincerely,

¹ NYLIFE Securities Inc. is a wholly owned subsidiary of the New York Life Insurance Company, the largest mutual life insurer in the United States.

² Securities Exchange Act Release No. 49148 (February 2, 2004), 69 FR 6438-01 (February 10, 2004) (File No. S7-06-04) (the "Release").

³ For purposes of this discussion, the term "mutual fund" also refers to Section 529 plan securities.

⁴ Securities Confirmations, Exchange Act Release No. 13508 (May 5, 1977).

⁵ 1979 WL 13637 (SEC No-Action Letter) (publicly available April 18, 1979).

⁶ 1994 WL 131068 (SEC No-Action Letter) (publicly available March 16, 1994).