April 9, 2004 **VIA Electronic Mail**

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

Re: Confirmation Requirements and Point of Sale Disclosure Requirements for Transactions in Certain Mutual Funds and Other Securities, File No. S7-06-04

Dear Mr. Katz:

1st Global Capital Corp. ("1st Global") is a fully disclosed retail broker-dealer registered to conduct business in all domestic jurisdictions, with over 1200 Registered Representatives offering securities services through nearly 600 branch and non-branch locations.

As the Chief Executive Officer of 1st Global, I appreciate the opportunity to submit comments on the issues raised in the above captioned Proposal by the Securities and Exchange Commission ("Commission"). I would be remiss in not mentioning my objection to the short comment period provided for such unprecedented Commission action.

As a threshold matter, it is important to state that I support enhanced disclosure for mutual fund investors. However, I believe that the Proposal, even by the Commission's own unrealistically low estimates, is far too expensive. The Proposal imposes a multi-billion dollar cost which will be borne primarily by small retail investors. The net result of the Proposal will be to make mutual funds less available and less attractive for small, beginning and unsophisticated investors – precisely the investors for whom mutual funds are often the most appropriate class of investment.[1] Moreover, the great costs which the Proposal would impose will provide little assistance to investors; in fact, the proposed disclosures will distract investors from the more important information in the fund prospectus. I want to stress that my disagreement with the Proposal is not over the need for improved disclosure – it is over how best and most cost-effectively to make that information available for investors.

Please note that before going into detail on our concerns with the Proposal, I wish to note my endorsement of the comments by both the Financial Services Institute and the Securities Industry Association.

[1] For ease of use, this comment letter generally will refer to "mutual funds," although I recognize that the Proposed Rules also cover UITs and 529 plan securities, and do not cover some closed-end or exchange-traded funds often referred to as mutual funds.

Proposal Is Simply Too Costly

The SEC's own estimate is that Rules 15c2-2 and 15c2-3 would cost the industry at least $1.3 billion to implement.[2] The SEC estimates that Rule 15c2-2 would cost the industry approximately $2 billion in annual recurring costs after initial implementation. The SEC estimates that this cost is $160 million more than the current Rule 10b-10 confirmations that Rule 15c2-2 rule would replace. And the SEC estimates that Rule 15c2-3 would impose an annual recurring cost of almost $1 billion.[3] All of the Rule 15c2-3 costs would be new costs for the industry. Including the costs of the remaining portion of Rule 10b-10, the SEC estimates that combined recurring costs for these rules (not including the initial implementation costs) will be nearly $7.5 billion per year.[4] By the SEC's own estimate, the year-one costs of these rules, including both the implementation cost and the first year of annual recurring costs, would be nearly $9 billion.

I believe that the SEC has substantially underestimated the cost of this rule Proposal. The SEC estimates that Rule 15c2-3, the point-of-sale proposal, would cost less than $85,000 for the average broker-dealer to implement, and would impose annual compliance costs of $180,000 per firm.[5] These estimates are substantially too low. The proposed rule would require firms like 1st Global to design a completely new system to create an entirely new written disclosure document and ensure that the disclosure document is available for distribution to clients at every location in which the firm meets with clients. It would require another system to ensure that the information in the disclosure document is available at every location where the firm accepts telephone calls from clients. It would require every firm that accepts mutual fund orders over electronic channels to reprogram all of those order-entry systems to give this disclosure before any

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[2] *See* Proposing Release, Initial Regulatory Flexibility Act Analysis Section D (sum of $850 million implementation cost estimate for Rule 15c2-2 and $450 million implementation cost estimate for Rule 15c2-3). The IRFA does not contain any implementation cost estimate for the changes to Rule 10b-10, although the Regulatory Flexibility Act requires the SEC to include such an estimate, and in fact the changes required by this proposed amendment are far from trivial. I would estimate an implementation cost of at least $100,000 per broker-dealer, for a total implementation cost of over $500 million.

[3] Id., see also Proposing Release, Costs and Benefits of the Proposed Rule and Rule Amendments.

[4] Id. at Costs and Benefits of the Proposed Rule and Rule Amendments (sum of $935 million in internal costs and $1.05 billion in external costs for Rule 15c2-2, $935 million in internal costs and $40 million in external costs for Rule 15c2-3, and $2.12 billion in internal costs and $2.26 billion in external costs for Rule 10b-10 as amended. The Commission estimates that the entire mutual fund industry can comply with the Form N1-A amendments for a combined cost of less than $100,000, which I believe is not a credible estimate for a substantial change that will, at a minimum, required substantial legal review by inside counsel, fund counsel and outside directors' counsel to ensure that it is correctly implemented.

[5] Id. at Initial Regulatory Flexibility Act Analysis.

order could be accepted. Moreover, every firm would be required to establish and monitor supervisory and compliance procedures to ensure that the disclosures are made in every customer interaction (including live meetings and telephone calls) before a mutual fund order is accepted.

In sum, I estimate that the implementation cost of this rule (even considering the number of very small brokerage firms) will be more on the order of $500,000 per firm, and the annual costs of maintaining and updating these systems and procedures will also be on the order of $500,000 per firm.[6] The SEC estimates that the confirm disclosure changes in proposed Rule 15c2-2 would impose an average one-time implementation cost of $157,000 per broker-dealer, and have an annual recurring cost of $368,000 per firm.[7] The cost of creating an entirely new confirmation statement with multiple new data feeds and complex new calculations personalized for every transaction plus the continuing cost of generating confirmations within the very compressed required time period is likely to be far higher than the SEC estimates. I believe that implementation costs of $500,000 per firm and ongoing annual costs of $750,000 per firm are will prove more realistic estimates than those in the release.[8]

Even under the SEC's own cost estimates, new rules 15c2-2 and 15c2-3 alone would have an annual cost nearly four times the SEC's entire annual budget. According to the SEC's own FOCUS reports, the entire U.S. brokerage industry's total annual revenue from mutual funds was $16 billion in 2002, and assuming the brokerage industry's average profit margin of 7.5% (again, the figure is derived from the SEC's own FOCUS reports),[9] the entire U.S. brokerage industry earned $1.2 billion in annual profits on mutual funds. Therefore the initial implementation cost of these Proposed Rules (under the SEC's own underestimates) is greater than the entire industry's 2002

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[6] My estimate would result in an implementation cost of almost $2.7 billion for Rule 15c2-3, and an annual ongoing expense of approximately $3 billion. As discussed below, my estimate that the point-of-sale disclosure will take an average of three minutes to discuss with customers, rather than the Commission's non-credible estimate of one minute, leads to the same $3 billion annual cost estimate.

[7] Id.

[8] My estimate would result in an implementation cost of almost $2.7 billion for Rule 15c2-2, and an annual ongoing expense of over $4 billion.

[9] The SEC's FOCUS reports do not have a separate "mutual funds expenses" line to compare to the "mutual funds revenue" line. My calculation of the overall brokerage industry profit margin is a comparison of overall revenues and overall expenses reported in the FOCUS reports. I am not aware of any evidence suggesting that the brokerage industry's profit margin is different on mutual funds than it is on other types of investments (although clearly mutual fund advisers have higher profit margins). Assuming a 10% profit margin on mutual fund business instead of a 7.5% profit margin would not materially change any of my conclusions.

annual profit from mutual funds. In addition, the annual recurring costs of these rules are also substantially larger than the entire industry's annual profits from mutual funds.[10]

Under the SEC's own cost estimates, these rules will cost more than $55 per year for each of the 54 million U.S. households that invest in mutual funds – or more than 5% of the annual savings of a typical middle-class household that is able to invest one thousand dollars per year in a mutual fund. The year-one costs, including both implementation and the first full year of ongoing costs, equate to almost $80 per household – or 8% of the savings of a middle-class household able to invest one thousand dollars per year in a mutual fund.

Analyzing the cost of the Proposal on a per-household basis is appropriate. While the initial costs may be borne by broker-dealers, it is reasonable to assume that we will have to pass that cost on to our customers. The cost will fall disproportionately on smaller investors, who already are the least profitable customers for most broker-dealers. Since the cost of these rules will be incurred primarily on a per-transaction basis, it will disproportionately weigh on small investors who are investing a small amount every month in a few mutual funds. The SEC can expect that these rules will cause broker-dealers to increase transaction fees for mutual funds (especially for small investors), as well as increase minimum balance sizes and increased periodic account service fees. The small retail consumer will be the loser, with higher costs and decreased access to professional investment advice. The SEC should have requested comments from the public about the Proposal's estimated costs. Would mutual-fund owning households be willing to pay $55 per year (and $80 in year one) for the type of disclosure mandated by the proposed rules? I suspect very few investors would answer yes.

The total cost of the rules would be far greater than the SEC itself estimates. My estimate (set forth above) would be that the annual ongoing expense of these rules equates to nearly $125 per household that owns mutual funds. The year-one cost (including both implementation costs and one full year of ongoing expense) equates to well over $200 per household. Again, I challenge the SEC to ask investors, especially small investors, whether they would voluntarily choose to pay this much for the SEC's proposed disclosure rules. If the rule is adopted, investors will not have the choice – they will be required to subsidize the cost of the rule.

The SEC does not attempt to quantify the expected benefit of the proposed rules. The Proposing Release states that the benefits "while qualitatively important, are necessarily difficult to quantify."[11] I believe that before the SEC imposes what is, even

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[10] I am aware of estimates that the mutual fund industry charges $13 billion annually in 12b-1 fees and $6.7 billion in sales loads. I believe these estimates are consistent with the SEC's FOCUS report numbers – a substantial portion of 12b-1 fees go to general advertising expenses for mutual funds, or to revenue sharing with retirement plans, banks or entities other than brokerage firms. Similarly, not all sales loads are earned by brokerage firms; for example, some contingent deferred sales loads are returned to the mutual fund complexes themselves.

[11] Proposing Release at Costs and Benefits of the Proposed Rule and Rule Amendments.

by its own calculation, a multi-billion dollar tax on American investors, it should be able to provide the public with a more convincing rationale for the Proposal's impact on retail investors.

I share the Commission's overall goal of improving investors' ability to make informed decisions when choosing to invest in mutual funds. However, I believe that there are alternatives far more effective and, more efficient to achieve this important goal.

Value of Prospectus Minimized

The Proposal discounts the prospectus as the primary disclosure tool in the offering of a security. It would seem that the Commission, through its actions, believes the prospectus has become of little value to the investor. One wonders how long it will be until the investor becomes numb from the sheer volume of data emanating from this Proposal. At some point, the Commission may come to view these new Proposals as valueless and some new "solution" will be proposed for the "problem."

In our view, the "problem" is the Commission's misperception that the general public lacks financial literacy. The Commission should note that this problem may not actually be a problem at all, it may be a choice. Perhaps the simple fact of the matter is that the majority of those who invest through intermediaries are doing so because they do not want to make the substantial investment of time it would take to gain the knowledge and skills necessary to identify and achieve their financial goals. When their Lexus is running poorly, they take it to a professional mechanic rather than obtaining a mechanics certification and repairing it themselves. When their roof leaks, they hire a professional roofing contractor to repair the roof rather than doing it themselves. When they want to invest, they hire a professional. Whether the Commission values the services provided by such professionals or not (and it seems that it does not), a substantial part of the population does value such service. Deluging these types of investors with additional information is not going to result in them making the determination that they need to invest their time to become an astute financial planner in order to implement an appropriate investment strategy.

Our society is one of specialists and no amount of disclosure is going to change that fact, i.e., this proposal is not going to effect the reliance that many individuals place on others to help them identify and achieve their financial goals. Additionally, the information that would facilitate educated questions in relation to such assistance is already available in the prospectus. For example, the sales charge and expenses are already disclosed in tabular format in the prospectus. Is it unreasonable to expect someone to open a prospectus? Rather than spending its time mandating unprecedented levels of duplicative disclosure, the Commission should expend its resources to ensure that only true professionals take part in the provision of financial services to the general public. Actions like requiring certain minimum levels of education for registered representatives and investment adviser representatives, increasing the degree of difficulty of entrance exams to the industry, mandating heightened levels of continuing education for registered representatives and investment adviser representatives, etc. will pay greater dividends than new disclosure-- disclosure that investors will quickly learn to disregard just like they disregard the current disclosure.

Disclosure is Redundant

The Proposal represents redundancy of disclosure in that the majority of the costs associated with purchasing a mutual fund are already detailed in the prospectus (and the remainder will be dealt with by the other SEC proposals which mandate the inclusion of all remaining cost elements in the prospectus). Disclosure of distribution costs is fundamentally the obligation of the mutual fund complex since it controls all of these costs and the myriad ways in which those costs are incurred. Prospectus disclosure can identify those costs and the fund's historical performance and cost data simply and accurately. The data gathering and administrative and disclosure burdens (and related liability for data errors) are being unfairly transferred to the brokerage industry. The SEC's reasoning may be that more detailed disclosure will force the industry to lower costs, and that lower costs will result in better investment performance. Of course, it is the mutual fund industry that controls those costs and there are many more variables affecting investment performance. One-time disclosure should be sufficient if the disclosure is made in writing. Given the cost associated with implementing the Proposal, there is little benefit in requiring disclosure of the same information three separate times, i.e. in the prospectus, at point of sale and on the confirmation.

Lack of Attention to Industry Structure

The Proposal also points to the Commission's lack of attention to a key attribute of the structure of the industry it regulates. The majority of broker-dealers that distribute mutual fund shares are introducing broker-dealers that clear their trades through a clearing firm and/or directly with the mutual fund company. In fact, the Proposal indicates that 5000 of the 5400 broker-dealers currently rely on another party's confirmation delivery system to fulfill their regulatory responsibility. In this light, the clearing firm and/or the mutual fund company supplies the client with confirmations and account statements on behalf of the introducing firm. The fact is that the data that supports this delivery system is not present at the introducing firm. Introducing firms will have to modify their systems to collect such data or will have to rely on the clearing firm and/or the mutual fund company to generate the point of sale disclosures.

This fact presents two problems. First, administratively this would require clearing firms and mutual fund companies to take action; however, such action on the part of clearing firms and fund companies is not required by the Proposal. If clearing firms and mutual fund companies choose not to take voluntary action with respect to the point of sale components of the Proposal, each of the 5000 introducing firms would be forced either (i) to internalize a function that is currently outsourced or (ii) to outsource to a third party provider at substantial cost. This Proposal should be amended to require compliance by clearing firms and mutual fund companies with respect to accounts custodied at the respective party. In the alternative, it should mandate that such parties provide the required disclosure information to introducing broker-dealers in a standardized format. Second, there are substantial assets custodied directly at the respective mutual fund companies ("retail direct business"). The Proposal should prohibit mutual fund companies from accepting any new retail direct business without first verifying that the appropriate point of sale disclosure has been provided to the client.

Right of Rescission Flawed

The Proposal's right of rescission is fundamentally flawed. Because the Proposal contemplates an unprecedented new point of sale disclosure regimen, it would fundamentally change the administrative process surrounding the distribution of mutual funds. It is unwise to add a right of rescission to an untested administrative process where all the variables may not be known or understood completely. The right of rescission component of the Proposal should be eliminated. Alternatively, this right should be tied to the failure to deliver the **confirmation,** not the **point of sale disclosure form**.

In summary, 1st Global opposes the Proposal in its present form because it (i) results in substantial costs, (ii) discounts the prospectus as the primary disclosure tool in the offering of a security, (iii) results in redundant disclosure in that the majority of the costs associated with purchasing a mutual fund are already detailed in the prospectus and the there are other SEC proposals to mandate the inclusion of all remaining cost elements in the prospectus, (iv) it underscores the Commission's lack of attention to a key attribute of the structure of the industry it regulates, i.e., that the majority of broker-dealers that distribute mutual fund shares are introducing broker-dealers that clear their trades through a clearing firm and/or directly with the mutual fund company, and (v) that the Proposal's right of rescission is fundamentally flawed. Without extensive substantive revision the Proposal will be disastrous for the industry and the individual investor who relies on mutual funds as his primary investment vehicle.

Again, we thank the Commission for the opportunity to comment on this important issue.

Sincerely,

/s/

Stephen A. Batman

CEO