Pershing
A BNY Securities Group Co.
Solutions from The Bank of New York

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VIA ELECTRONIC DELIVERY
AND FIRST CLASS MAIL

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

Re: Proposed Rule: Confirmation Requirements and Point-of-Sale Disclosure Requirements for Transactions in Certain Market Funds and Other Securities Security Act Rel. No. 8358 (January 29, 2004) (the "Proposing Release")

Dear Mr. Katz:

I write on behalf of Pershing LLC ("Pershing"), with respect to the above-referenced confirmation and point of sale disclosure rule proposal (the "Proposal"). Let me say at the outset that Pershing appreciates the opportunity to comment on the Proposal which (i) dramatically changes and expands mandatory disclosures in connection with the sale of open-end mutual funds and certain other products[1] and (ii) creates and imposes unprecedented pre-transaction point-of-sale disclosure requirements for mutual funds.

Pershing is a broker-dealer and member firm of the New York Stock Exchange, Inc which provides clearing services to approximately 1,100 broker –dealers and other financial organizations. Pershing applauds and supports enhanced disclosure of costs and of facts regarding potential conflicts of interest which may exist concerning the sale of mutual funds. Let me emphasize that its comments on the Proposal should not be seen as objecting to the principle of enhanced disclosure. Rather, Pershing believes that the Proposal may be difficult to implement, is unlikely to achieve the intended results in various respects, and imposes costly burdens that are inappropriate and unnecessary to achieve that objective. We also believe that implementation of the Proposal could take a substantial amount of time. These comments will be

[1] For convenience this letter will refer to mutual funds, but the comments refer to all of the products covered by the Proposal.

limited to certain aspects of the Proposal that are of particular concern to clearing firms.[2] As explained below, the Proposal is contrary to the well established division of responsibility between clearing firms and introducing firms, as permitted by New York Stock Exchange Rule 382, which was approved by the SEC in 1982, and as recognized in the long line of judicial and regulatory decisions that have followed in the ensuing two decades, including the SEC's recent decision in Del Mar Financial Services, Inc., Exh. Act Release No. 48,691 (October 24, 2003) (dismissing a charge against a clearing broker for allegedly aiding and abetting violations by an introducing broker).

A. Point-of-Sale Disclosure

The Proposal requires detailed disclosure, at each point of sale, by each broker-dealer involved in a mutual fund sale, before that transaction is effected. That disclosure would be required to include personalized and customized information setting forth precise amounts of front end loads, back end loads, sales fees, and asset-based service fees, as well as details on brokerage commissions, revenue sharing, differential compensation and breakpoints. The required disclosure is investment specific, and unique to each broker-dealer's relationship with the particular mutual fund complex whose product is purchased. Putting aside for the moment the wisdom of such point of sale disclosure (see SIA comment letter), the expense and difficulty of developing and maintaining the systems to gather, generate and continuously update that detailed information (see below), and the diversion of resources and effort that would be necessary to comply, no such requirement should be imposed on clearing firms, for the basic reason that clearing firms do not interact with customers at the point of sale, and have no role in the actual sale. Indeed, the clearing firm by contract and custom has no authority to interact directly with the ultimate customer or even to be present at the point of sale.

It is fundamental to the clearing relationship that front office services are provided by introducing brokers, while clearing firms provide back office services. Stated simply, sales are made by introducing brokers, not clearing firms. That is the basic reality and the time honored construct of Rule 382. Since the clearing firm has no role in a customer's investment decision, and is not even present at the point of sale, the disclosure of cost or other information by a clearing firm would not serve any legitimate disclosure interest.

Indeed, the Proposal recognizes this fact, as it would exempt from the point of sale disclosure requirement clearing firms that do not communicate with a customer other than to accept an order (Proposing Release pp.40-41). However, that is not where the Proposal stops. The Proposal goes on to condition that exemption on the clearing firm's "reasonable belief" that the introducing broker has delivered the required point-of-sale information, and then goes on to explain that a clearing firm's "reasonable belief" could be demonstrated if there is an agreement

[2] The Securities Industry Association ("SIA") has submitted extensive comments on the Proposal. Pershing endorses and adopts the SIA's comments, and will not burden you by repeating them here.

with the introducing broker requiring the introducing broker to deliver the required point of sale information, and if that agreement is "supplemented with appropriate auditing practices." It is these points that are particularly troubling.

Thus, under the Proposal, clearing firms are subject to the point of sale disclosure requirement, but may be able to avoid the need to deliver point of sale disclosure information by enforcing the separate obligation imposed on the introducing broker which actually makes the sale to its customers. This is a drastic change in the fundamental nature of the relationship between clearing firms and introducing brokers. It is unprecedented and, respectfully, unwise. Indeed, the magnitude of this departure from established practice is highlighted by the fact that requiring a clearing firm to audit compliance by an introducing broker with any legal or regulatory requirement does not exist in any context, including the USA Patriot Act.

Whatever point-of-sale disclosures may ultimately be determined to be appropriate, there is no basis to make clearing firms the auditors and, indeed, the guarantors, of compliance by introducing brokers.

The unfair and unnecessary burden this would impose on clearing firms is enormous. Under the Proposal, in addition to regulatory violations, transactions are subject to cancellation until the mandated point of sale disclosures are made. If the clearing firm has any responsibility in this regard -- and the Proposal does not even make the exemption certain -- it stands at risk of great loss if the introducing broker does not discharge its separate obligations. Customers could seek to cancel transactions on this basis and the clearing firm could stand at risk for resulting losses on cancelled trades. And, if the introducing broker's disclosure is later claimed to be inadequate, the clearing firm could potentially be the subject of customer claims or regulatory scrutiny on the basis of a claim that its audit was inadequate or its belief was unreasonable. This is further exacerbated by the fact that the Proposing Release states, repeatedly, that there is no safe harbor for violation of antifraud provisions. It is hardly difficult to imagine fraud claims being made against clearing firms based on allegedly inadequate disclosure by introducing firms, unless it is made clear that the point of sale disclosure obligation is the obligation of the introducing broker only.

This is a dramatic departure from long established law and an unnecessary and unjustified change in the fundamental relationship between clearing firms and introducing brokers. The simple and effective way to deal with whatever enhanced point of sale disclosure is ultimately determined to be appropriate, is to make clear that clearing firms that are not involved at the point of sale are not subject to that requirement, and have no audit or other obligation with respect to compliance by introducing brokers.

B. Confirmation Disclosure

The Proposal also dramatically changes the requirements with respect to information that

must be included on confirmations regarding the sale of mutual fund shares. The required information would include personalized and customized information for each customer's specific investment (on both a dollar and percentage basis) regarding front end loads, back end loads, sales fees, and asset based service fees, brokerage commissions, revenue sharing, differential compensation and breakpoints, as well as comparative data for industry medians and "similar" investments. This would impose an enormous burden on clearing firms to continuously gather, maintain and update this information, which will include information concerning relationships with all mutual fund complexes with which transactions are effected by any introducing broker.

As set forth in the SIA comment letter, this extensive expansion of confirmation disclosure is unnecessary and counterproductive. Clearing firms will bear the burden of developing and maintaining the new systems which will be required to perform complex and constantly changing calculations, and to generate the data to be reflected on confirmations. The cost of that endeavor is enormous and would have a negative effect on the industry and, ultimately, investors, with no real benefit to anyone.

C. The Negative Effect of the Proposal

The Proposal, if adopted, will dramatically change the relationship between clearing and introducing firms and will increase costs and divert time and resources from other areas. The Proposing Release recognizes that there will be a multibillion dollar implementation cost, as well as multibillion dollar recurring annual costs. These costs, which are dramatically underestimated in the Proposing Release (see SIA Comment Letter), will be borne in very great measure by clearing firms. Clearing firms will have to design and maintain multiple new systems, deal with information for themselves and for their individual introducing brokers, and covering the many mutual fund complexes with which any of them transact business.

Pershing notes that it currently has over 5 million active customer accounts and in calendar 2003 it processed over 4,100,000 mutual fund purchases. Each of those purchases could have required some number of point of sale disclosures as customers considered differing mixes of investments. While precise figures are not capable of precise calculation at this point, Pershing estimates that its implementation costs alone would exceed $500,000, and that its ongoing costs would exceed $500,000 per year. This burden is unfair and far beyond any benefit that the Proposal could hope to achieve.

D. Some Tentative Solutions

Pershing concurs with the SIA that a web site alternative has merit. The information could be available to potential investors in a convenient form and the inconvenience in having potentially hundreds if not thousands of conflicting, and potentially confusing, point of sale documents generated would be avoided. Pershing also believes that comparisons using a fixed amount to be invested, say $1,000 or $10,000 would be more meaningful to investors and would

be easier to implement.

When problems were identified in connection with the application of breakpoint sales for mutual funds, the industry, working with the NASD, mobilized to find solutions through the Breakpoint Task Force. Pershing was represented on that task force. We believe that a similar task force, including regulatory interests and the industry, could find workable solutions that enhance needed disclosure, control costs, do not upset the clearing broker-introducing broker relationship, and can be achieved in a timely fashion.

Conclusion

Pershing agrees with the SIA's explanation that the net effect on investors will be negative rather than positive. Pershing believes that enhanced disclosure is appropriate and supports the SEC's desire to provide meaningful information to investors. However, this must be done by carefully considering the information to be provided and the cost of doing so, in order to ensure that disclosure is achieved in a cost effective and sensible manner. Unfortunately, the Proposal does not do so. Pershing urges the SEC not to act rashly and to consider not only what disclosures should be required, but who should be required to make them.

We would be pleased to meet with the SEC to discuss these matters and to provide assistance in formulating additional means to ensure that investors receive the information they need to make informed investment decisions.

Respectfully,

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