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April 21, 2004

Jonathon G. Katz, Secretary
Securities and Exchange Commission
450 5th Street, N.W.
Washington, D.C. 20549

SUBMITTED ELECTRONICALLY: rule-comments@sec.gov

Re: Mandatory Redemption Fees for Redeemable Fund Securities (Release No. IC-26375A; File No. S7-11-04)

Dear Mr. Katz:

On behalf of ASPA, a national organization of over 5,000 retirement plan professionals, thank you for the opportunity to comment on the proposed new rule concerning mandatory redemption fees for redeemable fund securities under the Investment Company Act of 1940, as amended (Investment Company Act), which was recently proposed by the Securities and Exchange Commission (Commission). ASPA commends the Commission for its efforts to curb abusive short-term trading, or "market timing," in shares of mutual funds that harm long-term mutual fund investors, including participants and beneficiaries of tax-qualified 401(k) and similar tax-qualified defined contribution retirement plans (plans). As you are aware, most working Americans own their mutual fund investments through such plans.

ASPA recognizes that any measures adopted by the Commission to address abusive short-term trading must extend to transactions directed by participants of participant-directed plans. However, the imposition of inconsistent mandatory redemption fees under the current version of the proposed rule will create substantial confusion for plan participants. Further, the related financial intermediary information reporting requirements will result in significant and unnecessary plan administrative and other costs, which will ultimately be borne by plan participants. These administrative issues and increased costs could be substantially mitigated, without impacting the effectiveness of measures to address abusive short-term trading, by adding provisions under the proposed rule that take into account the special nature of participant-directed plans. In particular, ASPA urges the Commission to consider:

- Limiting the application of redemption fees and information reporting requirements to participant-directed "exchanges" and "transfers," which are the only transactions in plans susceptible to late-day trading;
- Establishing uniform standards for redemption fees applicable to participant-directed plans, including a standardized redemption fee percentage and holding period; and
- Providing for a mandatory *de minimis* exception that applies for both redemption fee purposes as well as the related reporting requirements.

The following is a more detailed discussion of these points and some additional comments on the proposed rule.

I. Background

A. ASPA. ASPA's membership consists of over 5,000 retirement plan professionals who assist employers in establishing and maintaining retirement plans for their workers. Its members include senior representatives from all sectors of the retirement plan marketplace, including independent "third party administrators," and banks, trust companies and insurance companies, that provide recordkeeping and other plan administration services (plan recordkeepers and administrators). Virtually all of the retirement plans in the United States are administered by firms that count ASPA members among their employees. From this perspective, ASPA is well-qualified to comment on the proposed rule's potential impact respecting retirement plans.

B. Role of Participant-Directed Plans in Retirement Savings. Participation in employer-sponsored participant-directed retirement plans has exploded over the last decade. DOL estimates that there are some 730,000 private sector pension and 401(k) plans, covering some 102 million individuals.[1] The majority of employees today who participate in any retirement savings plan have a defined contribution plan as their primary retirement savings vehicle. Therefore, these plans now play a critical role in the retirement savings of American workers. Plan recordkeepers and administrators have played an important role in this growth.

The Commission notes that approximately one third of mutual funds shares are held through retirement plans.[2] ASPA believes that this substantial investment of plans' assets in mutual funds has been possible in significant part because plan recordkeepers and administrators have developed efficient recordkeeping and order processing systems that allow cost-effective delivery of plan administration and transaction processing services, even where participants have small account balances and make small dollar value

[1] U.S. Department of Labor, Employee Benefits Security Administration, "Labor Department Issues Guidance on Fiduciary Duties In Response to Mutual Fund Abuses," Feb. 17, 2004 (Media Release), available at www.dol.gov/ebsa. These numbers do not include an additional substantial number of tax-qualified participant directed plans sponsored by various governmental entities and church organizations.

[2] 69 Fed. Reg. at 11764 n.17.

periodic contributions. In this regard, plan participants making very small periodic contributions or with small account balances generally would not be eligible to invest in many mutual funds, which often impose minimum requirements for investor accounts, or would be able to do so only at substantially more cost. (For example, plans may invest in lower-cost "institutional" share classes, which would not be offered to participants as individual investors.)

Any measures that the Commission takes to address market timing must recognize the value of current plan recordkeeping and order processing systems in facilitating the retirement savings of ordinary Americans. Accordingly, in addressing abusive market timing in mutual funds, the Commission should seek to preserve the efficiencies and cost savings provided by these systems as much as possible.

C. Typical Plan Investment Structure. Generally, tax-qualified defined contribution retirement plans, including 401(k) and similar plans, do not promise participants a specific amount of benefits at retirement. Instead, while participants are employed by the employer plan sponsor, participants or the employer (or both) contribute to "individual accounts" maintained for each participant under the plan. The contributions are held and invested on behalf of participants, and each participant ultimately receives a benefit based on the amount of contributions made to his or her individual account, plus or minus investment gains and losses, plan expenses, and other adjustments provided by the plan.

If the plan is designed to be participant-directed, participants generally direct the plan trustee, or another plan fiduciary, on how their contributions and account balances should be allocated among a selection of plan investment alternatives.[3] The investment alternatives are selected by a "fiduciary" of the plan (plan fiduciary), who must select and monitor the plan's investment alternatives prudently.[4] The plan fiduciary generally retains

[3] Some defined contribution plans do not allow participant direction—instead, the trustee or other plan fiduciary, or a plan investment manager, determines how plan assets are invested.

[4] Private sector 401(k) and similar plans are subject to Employee Retirement Income Security Act of 1974 (ERISA), which requires (among other things) that plans be operated in accordance with governing plan documents naming one or more "fiduciaries" charged with the management and operation of the plan. See ERISA §402. These fiduciaries include an "administrator," "trustee" and other "named" fiduciaries. Under ERISA section 3(16), the "administrator" is responsible for the overall administration of the plan. The employer plan sponsor is the plan administrator unless the plan names a different plan administrator. (A professional plan recordkeeper or administrator is almost never named as a fiduciary administrator of a plan; in fact, in most cases, professional plan recordkeepers and administrators do not perform any functions that could cause them to be "fiduciaries" of a plan.) The plan "trustee" is responsible for management and control of plan assets. See ERISA §403(a). The plan trustee may be a financial institution, or (particularly in the case of small plans) instead may be an individual employed by the employer plan sponsor. If a financial institution is trustee, it may be a "directed trustee" that generally acts only upon directions from a "named fiduciaries" or an investment manager. Plans often provide for a separate "named fiduciary" that is responsible for plan investment matters, such as the selection and monitoring of plan investment alternatives. Other persons may become plan fiduciaries, if they perform one or more "fiduciary" functions, as defined by ERISA section 3(21).

authority to direct plan investment transactions affecting a participant's account for certain reasons, such as where changes to plan investment alternatives will be made. If a participant does not provide affirmative investment instructions as to the investment of the participant's account, a plan fiduciary must determine how the participant's account is allocated among plan investment alternatives.

As participant-directed retirement plans have developed in recent years, it has become common that a plan's investment alternatives are managed by a variety of unaffiliated investment managers and distributed by different fund complexes under an "open architecture" model. One reason for this development is that plan recordkeepers and administrators are not affiliated with mutual fund investment managers and thus chose to provide plans access to a broad, diversified selection of mutual funds and other investment options. Today, even plan recordkeepers and administrators that are affiliated with large mutual fund complexes typically make their competitors' mutual funds available to plan clients. These mutual funds may even be combined to provide custom portfolio (fund of funds) options for participants. ASPA believes that this trend provides important benefits to plans and participants because plan fiduciaries may select from a broad range of mutual funds to obtain the best combination of investment performance and cost for plan participants.

D. Types of Plan Investment Transactions. In the ordinary course of operating a participant-directed defined contribution plan, the plan may engage in investment transactions for a variety of reasons and purposes. All of these plan transactions are governed by specific rules described in governing plan documents and must also comply with statutory requirements under the Internal Revenue Code of 1986, as amended (Code). Except where the employer sponsor is a governmental entity or a church organization, the plan is also generally governed by the Employee Retirement Income Security Act of 1974, as amended (ERISA).

1. Contributions. Plans may purchase mutual fund shares upon receipt of new plan contributions from participants or the employer. In this regard, participants typically contribute periodically by payroll deduction at a set rate (*e.g.,* 5% of earnings annually), although these contributions are subject to an annual statutory limit.

Employers may "match" participant contributions, or contribute specific amounts on an annual basis, or make discretionary contributions in accordance with the plan's terms. Some plans also allow participants to make additional contributions by making a "rollover" from another tax-qualified plan, or a "rollover" individual retirement account, under certain limited conditions.[5]

2. Distributions and Withdrawals. Plans redeem mutual funds shares if the participant takes a withdrawal or distribution of benefits from the plan. Generally, participants may withdraw or receive a distribution from their defined contribution plan

[5] The current stockholder annual limit on employee payroll contributions is $13,000. See Internal Revenue Code section 402(g).

accounts only upon termination of employment or retirement. Plans may also permit participants to "in-service" distributions because of hardship, or for other reasons, under certain conditions. Under certain circumstances, a plan may be required to distribute some or all of the participant's account (*e.g.,* under mandatory "cash-out" rules for account balances of $5,000 or less and under mandatory distribution rules for participants reaching age 70½). Participants taking a withdrawal or distribution cannot "reinvest" amounts received in the plan. All of these transactions are governed by detailed plan rules as well as regulations under the Code, which strictly limit the circumstances under which participants can receive withdrawals and distributions from a plan.

3. Loans. Plans may redeem mutual fund shares if a participant requests a loan. Plan loans are statutorily limited to one-half of the value of a participant's account, subject to a maximum of $50,000.[6] As the participant repays the loan, the plan will purchase new shares with the loan repayments, in accordance with the participant's investment instructions for payroll contributions. Typically, loan repayments are made by payroll deduction.

4. Transfers and Exchanges. Plans may purchase and redeem shares of mutual funds to effect a participant's instructions to change the allocation of the participants' accounts among plan investment alternatives. These "exchanges" or "transfers" may include exchanges or transfers resulting from "rebalancing" transactions.

5. Fiduciary-Directed Transactions. Plans also may redeem or purchase shares as a result of plan fiduciary directions, such as the termination or substitution of one or more plan investment alternatives after a periodic plan investment review, custom portfolio (fund of funds) rebalancing, or a conversion to a new plan services arrangement.

II. Redemption Fees Should Only Apply to Transfers and Exchanges

Under the proposed rule, mutual funds would be required to impose a 2% redemption fee upon the redemption of mutual fund shares purchased in the previous five days. The proposed rule would also require "financial intermediaries" to assist mutual funds in identifying and collecting redemption fees and to provide weekly reports of all fund shareholder trading activity. ASPA understands that, in the case of participant-directed plans, the Commission intends that the mandatory redemption fee and the information reporting requirements will apply in connection with transactions processed for each participant account under the plan.

Implementing these new requirements and administering the requirements on an ongoing basis will result in substantial additional plan administrative costs that will be borne by plan participants. In addition, the current form of the proposed rule would impose redemption fees for plan transactions that do not provide an opportunity for market

[6] See Internal Revenue Code section 72(p).

timing. For example, if a participant's payroll contributions are invested in one or more mutual funds on Day 1, and the participant requests a loan transaction on Day 3, shares redeemed to fund the loan payment could be subject to redemption fees. Similarly, if a participant's rollover contributions are received under a plan on Day 1 and the plan fiduciary makes changes to plan investment alternatives that result in redemptions of shares owned by the plan on Day 4, redemption fees could be imposed. In both cases, imposition of a redemption fee would be plainly unfair.

The Commission can address these concerns about the initial and ongoing costs of the proposed rule, as well as its unfair application to routine plan transactions that do not provide an opportunity for market timing abuse, by adopting special provisions so that the proposed rule's redemption fee and information reporting requirements only apply to participant-directed exchanges and transfers between plan investment alternatives. This approach would protect mutual fund investors against abusive trading by plan participants, while substantially reducing the adverse impact and administrative costs of the proposed rule.

In this regard, of all of the types of plan investment transactions described above, only participant-directed exchanges and transfers provide any opportunity for abusive frequent or excessive trading by plan participants. For example, participants do not have the capability to "time" mutual fund share purchases in connection with payroll contributions or periodic loan repayments because the timing of these purchases depends upon when the employer deposits the funds into the plan, and the contributions are invested according to standing participant instructions. Any rollover contributions or lump sum loan repayments by a participant typically require at least one or more days processing time upon receipt by the plan trustee and recordkeeper; therefore, a participant would not be able to "time" purchases of mutual fund shares in connection with these transactions. Also, where plan transactions are directed by a plan fiduciary (*e.g.*, to effect changes in the plan's investment alternatives or rebalance a custom portfolio), the participant also does not provide a direction and could not "time" share purchases or redemptions.

Plan rules may allow a participant to determine the timing of share redemptions under a plan to fund loans, withdrawals or distributions. Nevertheless, these transactions also do not provide opportunity for market timing abuse. In this regard, participants must be eligible for withdrawals and distributions under plan rules and cannot reinvest the withdrawal or distribution proceeds through the plan. Significantly in the case of withdrawals and distributions other than plan loans, the amount would potentially be subject to ordinary income tax rates and possible penalty taxes in the year received, greatly deterring market timing abuse. In the case of a loan, participants cannot "time" the reinvestment of loan repayments because the repayment is typically made by periodic repayments. If the participant makes a lump sum repayment, at least one or more days processing time for reinvestment removes the participant's opportunity to "time" the loan repayment. Also, the reinvestment typically would be implemented based on a participant's standing instructions for the reinvestment of new plan contributions, further adding to the difficulty of using these types of transactions to engage in market timing activities.

Therefore, to address market timing by plan participants, the Commission need only address its regulation of plan transactions to participant-directed exchanges and transfers. Specifically, only participant-directed exchanges and transfers in a participant-directed plan should need to be monitored to determine whether any redemption fees should be assessed, and financial intermediaries should only need to report to mutual fund companies participant-directed exchange and transfer transactions under a plan.

Importantly, this approach would provide substantial relief to plans (and also to mutual fund companies) from the administrative costs and other burdens that would be caused by the proposed rule in its current form. For example, one large recordkeeping firm has reported to ASPA that, of the 1 billion participant "events" (*i.e.*, contributions, loans, withdrawals, etc.) that it processes annually, only about 16 million (1.6%) involve exchanges or transfers. Over the entire retirement plan marketplace, ASPA estimates that easily between 12-15 billion individual participant transactions would need to be reported annually to mutual fund companies under the proposed rule. In terms of systems cost, this is not insignificant and will have a major impact on participant fees. Plainly, the number of transactions that would need to be monitored in order to impose redemption fees and for information reporting purposes under the proposed rule would be significantly reduced. By limiting the imposition of redemption fees to only those transactions likely to result in abuse, it will provide significant savings to plans, plan participants, as well as mutual fund companies.

The Commission has already recognized that participant-directed transactions, other than exchanges and transfers under tax-qualified participant-directed plans, should be exempt from other regulations that address potentially abusive trading. In particular, Rule 16b-3(c) under the Securities Exchange Act of 1934 (Exchange Act) exempts from the short-swing profit recovery provisions under section 16 of the Exchange Act transactions by participants under "tax-conditioned plans" (including tax-qualified 401(k) and similar plans) other than "Discretionary Transactions" such as "fund-switching" or intra-fund transfers.[7] This exemption was premised on the view that adequate safeguards exist

[7] 17 C.F.R. §240.16b-3. Ownership Reports and Trading by Officers, Directors and Principal Security Holders, Release No. 34-37260 (May 31, 1996), 61 Fed. Reg. 30376 (June 14, 1996). Rule 16b-3 defines "Discretionary Transaction" as "a transaction pursuant to an employee benefit plan that: (i) Is at the volition of a plan participant; (ii) Is not made in connection with the participant's death, disability, retirement or termination of employment; (iii) Is not required to be made available to a plan participant pursuant to a provision of the Internal Revenue Code; and (iv) Results in either an intra-plan transfer involving an issuer equity securities fund, or a cash distribution funded by a volitional disposition of an issuer security." The definition of "Discretionary Transaction" would include participant-directed "intra-plan" exchanges and transfers involving equity securities offered under a plan, and also loans and in-service distributions funded by a sale of equity securities. The definition specifically excludes transactions in connection with a participant's death, disability, retirement or termination of employment on the basis that "[a]lthough such transactions have an element of volition, the insider's opportunity to speculate in the context of death, disability, retirement or termination of employment would seem well circumscribed." 61 Fed. Reg. at 30380. ASPA believes that, in the context of restrictions intended to address abusive market

against "speculative abuse" when a plan satisfies conditions imposed under the Internal Revenue Code and ERISA, and therefore, "routine" plan transactions should be exempt.[8] Similarly, Rule 16a-3(g)(1) provides relief from insider reporting requirements under section 16(a) of the Exchange Act for transactions in issuer equity securities that are exempted by Rule 16b-3(c). Plan transactions exempted by Rule 16b-3(c) are also exempted under the Commission's regulations under Section 306(a) of the Sarbanes-Oxley Act of 2002 (prohibiting executive officers and directors of an issuer from purchasing or selling issuer equity securities during a pension plan blackout).[9]

III. Uniformity is Necessary

As the Commission recognizes, implementation and ongoing administration of the redemption fees and the information reporting requirements under the proposed rule are expected to result in substantial costs. In the case of participant-directed plans with an "open-architecture" investment structure, these costs will be further magnified if mutual fund companies are permitted to impose redemption fee structures as well as other restrictions to curb market timing.[10]

Specifically, a typical participant-directed plan that includes mutual fund investment alternatives offered by several fund complexes could be faced with the possibility that each mutual fund investment alternative offered by the plan could impose different redemption fee procedures. For example, each mutual fund could be subject to including longer or shorter holding periods, "tiered" redemption fees (*e.g.*, 2% for a short holding period and then 1% for redemptions within a longer holder period), and different procedures for applying a *de minimis* standard. Implementing all of these various restrictions would greatly increase costs and make it difficult on an ongoing basis to ensure that the applicability and fee amount are correctly determined in each case. Moreover, all of the different restrictions must be communicated to plan participants, who are likely to find the restrictions confusing when each fund is subject to different rules. The effect of this likely confusion should not be underestimated. Retirement plan participants will get increasingly frustrated with non-uniform redemption fee structures negatively impacting their confidence in the retirement plan as an effective investment vehicle. Significantly, the existence of non-uniform redemption fee structures will create a competitive disadvantage for retirement plan administrators and intermediaries who offer "open architecture" multiple fund family platforms relative to mutual fund companies providing retirement plan services that offer only a single family of funds.

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timing, plan rules and administrative restrictions similarly circumscribe participants' opportunity to engage in abusive market timing through payroll contributions, loan transactions and in-service distributions.

[8] 61 Fed. Reg. at 30379.

[9] 17 C.F.R §245.101(c)(2).

[10] Indeed, the Commission recognizes that mutual funds, if allowed, will be likely to impose additional restrictions to curb market timing. 69 Fed. Reg. at 11767.

These problems can be addressed, however, if the Commission adopts a set of uniform procedures for the application of redemption fees to participant-directed plans. In particular, ASPA urges the Commission to adopt the following as uniform rules for participant-directed tax-qualified defined contribution plans.

- Redemption fees should be uniformly set at 2% (or at another appropriate level as determined by the Commission). For example, plans should not be permitted to impose a higher or lower redemption fee, or to impose "tiered" fees (*i.e.,* a 2% fee charged on redemptions within five days and a 1% fee charged on redemptions after the five days, but within 90 days).

- A standard holding period should be set for participant-directed transactions. If the Commission concludes that a holding period longer than five days is appropriate, ASPA urges the Commission to adopt the longer holding period on a uniform basis rather than allowing funds to define different holding periods that increase administrative complexity and plan participant confusion.

- The proposed *de minimis* exception provision should be mandatory and uniform, at least with respect to transactions in participant-directed plans. Specifically, the Commission should require mutual funds to waive the assessment of redemption fees if the amount of shares redeemed is under a certain threshold. In addition, ASPA encourages the Commission to adopt a *de minimis* threshold under which redemption fees and mandatory participant level reporting only would apply if the amount redeemed is greater than $5,000. It is extremely unlikely that transactions below this amount would involve potential market timing abuses to be of any concern to the Commission.

IV. Other Comments

A. Information Reporting Requirements. As noted above, the number of transactions for participant accounts under a participant-directed plan that occur during the course of a year is overwhelmingly large. An important question is whether all of the information associated with these transactions must be transmitted and whether mutual fund companies will be able to analyze such information.

Due to the substantial costs associated with the information reporting requirements under the proposed rule, ASPA strongly urges the Commission to limit the information that mutual funds receive in the case of participant directed plans to information about participant-directed exchanges and transfers that exceed the dollar threshold for imposing redemption fees under the *de minimis* exception.[11] Although this would substantially

[11] The impact of the extensive and burdensome participant-level reporting requirements contained in the proposed rule, as discussed in Section II above, would be somewhat ameliorated if the *de minimis* exception applied for such reporting requirements. So, for example, payroll contributions, which constitute

reduce the total amount of information that mutual fund companies receive, ASPA believes that mutual fund companies would still receive the transaction information they would need to determine whether the fund's market timing policies are successful and to better enforce their policies consistent with the intent of the Commission's rule.[12]

B. Omnibus Trading. ASPA appreciates the Commission's stated intent, as reflected in the proposed rule, to design an impediment to market timing that will enable intermediaries and retirement plan administrators to continue to trade on an omnibus basis.[13] ASPA is aware that there are some commentators who have suggested to the Commission that they consider eliminating omnibus trading as a way to prevent market timing. On behalf of the retirement plan industry, we wish to strenuously assert our objection to any restrictions on the ability of intermediaries and retirement plan administrators to trade on an omnibus basis that might be contained in the final rule.

As discussed earlier, employer-sponsored retirement plans have been the most effective means of providing working Americans with a low-cost vehicle for investing. The economies of scale obtained through omnibus trading have been a major factor in this regard. Any restriction on or elimination of omnibus trading would substantially diminish the benefit of this efficiency.

Using the large retirement plan administrator example above, the elimination of omnibus trading would require that administrator to process approximately 1 billion trades a year. Through omnibus trading, the number of trades actually processed annually is less than 400,000. That is an enormous savings in terms of transaction costs, which is passed on to plan participants. Without omnibus trading, participant fees will substantially rise ultimately leading to reduced retirement savings and likely reduced savings participation rates.

C. Proposal to Delay the Determination Net Asset Value for Transactions. The Commission requested comment on whether it should require funds to determine the value of purchase and redemption orders for mutual funds at the net asset value

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a substantial majority of retirement plan transactions, would no longer have to be reported. However, ASPA continues to believe that the further exceptions suggested in Section II should be adopted by the Commission for the reasons provided.

[12] ASPA understands that with respect to possible rules designed to eliminate late day trading, the Commission is evaluating the details of a clearing agency alternative to the so-called "hard 4 p.m. close." We also understand that the clearing agency alternative contemplates that real-time participant-level trade information, involving all retirement plan transactions other than basic payroll contributions, will be sent to the National Securities Clearing Corporation (NSCC), and that such information will be shared with the affected fund companies. To the extent this is the case, ASPA would urge the Commission to consider a blanket exemption from all reporting requirements contemplated under this proposed rule to curb market timing abuses for all trades submitted to the NSCC since any such reporting requirements would be unnecessarily duplicative of the information already sent.

[13] 69 Fed. Reg. at 11764.

calculated the next day after it receives orders, rather than the next time that the fund next calculates net asset value.[14]

ASPA believes that this approach would substantially diminish the ability of plan participants to promptly effect their plan investment decisions. Further, given the volatility of today's markets, this approach would deny plan participants the ability to make their investment decisions based on current market information. This result would be particularly problematic since large investors, investing directly in stocks, bonds or other securities, or even though exchange-traded funds, would be able to trade on current market information ahead of mutual fund investors. Therefore, ASPA respectfully suggests that the Commission reject this approach on the basis that it would harm rather than protect small investors, such as retirement plan participants.

In conclusion, ASPA agrees that measures to address abusive market timing must also apply to transactions directed by participants of participant-directed plans. However, it is important that the Commission adopt measures tailored to the special nature of participant-directed defined contribution plans and that facilitate rather than hamper the effective administration of these plans. Therefore, ASPA urges the Commission to consider changes to the proposed rule, including limiting the application of redemption fees and information reporting to participant-directed exchanges and transfers, and setting uniform rules for redemption fees imposed upon the redemption of fund shares by participant-directed plans.

D. <u>Next-Day Pricing.</u> In the proposed rule, the Commission asks whether it should consider mandatory next-day pricing for mutual funds as a means for preventing late-day trading. We strongly urge the Commission to dismiss such a method for preventing market timing. As we pointed out in detail in our comments in response to the Commission's proposed rules designed to prevent illegal late-day trading, retirement plan investors have come to expect that they will have the ability to trade at the same day's price provided their order is submitted timely. This has become increasingly important in recent years as mutual fund and other Wall Street scandals have come to light. Retirement plan investors want to know that they will have the ability to react quickly in the face of a possible scandal that is revealed in the media. If the ability to respond promptly to a scandal is taken away by mandating next day pricing, we believe that will further erode the already shaken confidence of the average retirement plan investor.

E. <u>Technical Comments.</u> ASPA understands that the Commission intends that mandatory redemption fees and information reporting requirements under the proposed rule will apply to transactions directed by participants under participant-directed plans. However, the proposed text of the rule is not clear about this.

First, section (a) of the proposed rule provides that a redemption fee is charged when shares are redeemed within five days of purchase, but does not distinguish that, in the

[14] 69 Fed. Reg. at 11768.

case of a participant-directed plan, the purchase and redemption transactions that are monitored for this purpose must be directed by the same participant. In this regard, a plan trustee acting on behalf of a participant-directed plan is typically viewed as the "shareholder" of mutual fund shares held by a plan. Thus, one reasonable reading of proposed Rule 22c-2 would be that shares redeemed by the plan within five days of purchase are subject to a redemption fee, even if the purchase and redemption transactions result from directions of different plan participants. Because of this, ASPA believes that this section of the proposed rule should be revised by adding that, in the case of a participant-directed plan, the redemption fee applies only to redemptions resulting from instructions by the same plan participant who directed a purchase of shares by the plan within the previous five days (or other holding period as determined by the Commission).

Second, it is unclear who has the "financial intermediary" obligations under the proposed rule. In this regard, the proposed rule defines the term "financial intermediary" to mean a "record holder" as defined in Rule 14a-1(i) under the Exchange Act and an insurance company that sponsors a registered separate account organized as a unit investment trust. See Proposed Rule 22c-2(f)(1). Rule 14a-1(i) defines a "record holder" to mean "any broker, dealer, voting trustee, bank, association or other entity that exercises fiduciary powers which holds securities of record in nominee name or otherwise or as a participant in a clearing agency registered pursuant to section 17A of the Act."[15] Rule 14a-1(c) defines "entity that exercises fiduciary powers" to mean "any entity that holds securities in nominee name or otherwise on behalf of a beneficial owner. . . ."[16]

The term "beneficial owner" is not defined by the proposed rule, or under Rule 14a-1. Rule 14b-2 under the Exchange Act defines "beneficial owner" to mean the person who has or shares, pursuant to an instrument, agreement or otherwise, the power to vote, or to direct the voting of a security.[17] However, it is common under participant-directed plans for a plan trustee and not participants to have voting responsibility for mutual fund shares. Therefore this definition would, in many cases, not achieve the result that participant-directed transactions are subject to redemption fees. Some no-action letters issued by the staff of the Division of Investment Management take the position that plan participants are "beneficial owners" where they direct the investment of their individual accounts under certain conditions.[18] However, given that there are various definitions of

[15] 17 C.F.R. §14a-1(i).

[16] 17 C.F.R. §14a-1(c).

[17] 17 C.F.R. §14b-2(a)(2).

[18] See PanAgora Group Trust (pub. avail. Apr. 29, 1994) (staff took position that, for purposes of determining compliance with Investment Company Act section 3(c)(1), each participant in a participant-directed plan who invests through the plan in a generic option consisting of a "section 3(c)(1) fund," and decides whether or how much to invest in the section 3(c)(1) fund, should be treated as a single "beneficial owner" of the section 3(c)(1) fund, for purposes of determining whether the fund meets the requirement to have 100 or fewer beneficial owners).

the term "beneficial owner," ASPA believes that this interpretative position, if applicable, should be incorporated in the proposed rule.

Third, assuming that participants of participant-directed plans are "beneficial owners," the definition of "financial intermediary" provided in the proposed rule would appear to mean a plan trustee responsible for holding mutual fund shares in trust on the plan's behalf. However, typically, this plan trustee, particularly in the case of small business retirement plans, is not responsible for maintaining any participant account records, or receiving and processing participants' instructions for the allocation of their individual plan accounts among plan investment alternatives. Instead, this information is typically maintained by a plan recordkeeper engaged by the "administrator" of the plan.[19] Therefore, the rule will place the information reporting burdens under the rule on an entity (or in the case of some plans, an individual) who may not maintain the information required to be provided to mutual fund companies.

The Commission may wish to consider whether the "financial intermediary" obligations, in the case of participant-directed plans, might better be placed with the plan recordkeeper entity that has responsibility to process and transmit orders to mutual funds on behalf of the plan. Typically, this entity (unless an affiliate of a financial institutional acting as plan trustee) does not hold the plan's shares as a "record owner" and therefore, would not be a "financial intermediary" under proposed Rule 22c-2(f)(1). However, plan recordkeepers and administrators have access to the information that is required to be provided to funds under the proposed rule and also often have direct or indirect contractual relationships with the mutual funds under which they receive and process orders for the fund's shares.[20]

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Thank you for your consideration of these comments. We commend the Commission and its staff for its efforts to address abusive market timing by mutual fund investors, while taking into account the concerns of the retirement plan industry. We are available to discuss these comments and any other questions that may arise as you continue to consider these issues.

Sincerely,

/s/	/s/	/s/
Brian H. Graff, Esq.	Jeffrey C. Chang, Esq., Co-chair	Sal L. Tripodi, Esq., Co-chair
Executive Director	Government Affairs Committee	Government Affairs Committee

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[19] See note 5, *supra*, describing the roles and responsibilities of the "trustee" and "administrator" of ERISA-covered plans.

[20] The Commission's estimates of costs in connection with the proposed rule in fact take the approach that "financial intermediaries" who would be required to transmit information to funds under the proposed rule are banks, insurance companies, and retirement plan administrators. 69 Fed. Reg. at 11770.