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June 6, 2005

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

Re: Mutual Fund Redemption Fees, File No. S7-11-04, 70 Federal Register 13328 (March 18, 2005)

Dear Mr. Katz:

The American Bankers Association[1] ("ABA") appreciates the opportunity to provide comments on the request of the Securities and Exchange Commission's ("Commission") for additional comments in connection with the final adoption of Rule 22c-2. That Rule would allow but, not require, registered open-end investment companies ("funds") to impose a redemption fee, not to exceed two percent of the amount redeemed, to be retained by the fund. The fee is designed to allow funds to recoup some of the direct and indirect costs incurred as a result of short-term trading strategies, such as market timing.

Rule 22c-2 also requires each fund to enter into written agreements with its financial intermediaries, including those holding shares in omnibus accounts, providing the fund with access to information about transactions by fund shareholders. Under the rule, the agreement must also contain a provision requiring the intermediary to execute the fund's instructions to restrict or prohibit further purchases or exchanges by any shareholder identified by the fund as having engaged in trading that violates the fund's market timing policies. In recognition of the additional systems and compliance programs that need to be developed, full compliance with the rule will not be required until October 16, 2006.

As investors in mutual funds, either for our own portfolio or for that of our fiduciary and brokerage clients, we support the Commission's efforts to protect mutual

[1] The American Bankers Association, on behalf of the more than two million men and women who work in the nation's banks, brings together all categories of banking institutions to best represent the interests of this rapidly changing industry. Its membership—which includes community, regional and money center banks and holding companies, as well as savings associations, trust companies and savings banks—makes ABA the largest banking trade association in the country. The views in this letter are also endorsed by the ABA Securities Association ("ABASA"). ABASA is a separately chartered trade association and non-profit affiliate of the ABA whose mission is to represent before the Congress, the federal government and the courts the interests of banking organizations engaged in underwriting and dealing in securities, proprietary mutual funds and derivatives.

fund investors and to restore investor confidence in mutual funds. With respect to new Rule 22c-2, we would like to address some of the issues raised by the adoption and concomitant request for comment from the viewpoint of banks that provide services as intermediaries.

Discussion

As the Commission has recognized, many investors' holdings in mutual funds are held through omnibus accounts generally denominated in the name of the broker-dealer, bank, insurance company, or retirement plan intermediary. Many of our members or their affiliates serve as broker-dealers, bank and savings association fiduciaries and retirement plan recordkeepers. For example, almost 2,000 banks, savings associations and trust companies serve as fiduciary or custodian for over 40 million accounts collectively valued to hold assets in excess of close to $50 trillion.[2] A very large proportion of that $50 trillion in assets is invested in mutual fund shares. Obviously, Rule 22c-2 is of great interest to our members.

Shareholder Transaction Information

As noted above, new Rule 22c-2 requires funds, regardless of whether the fund imposes a redemption fee, to enter into written agreements with their intermediaries under which the intermediaries must, upon request, provide funds with certain shareholder identity and trading information. This requirement will enable funds to obtain the information that they need to monitor the frequency of short-term trading in omnibus accounts and enforce their redemption fee policies. Because banks and other financial intermediaries will be contractually bound to provide transactional information to all mutual funds with which they do business,[3] even for funds that have chosen not to impose a redemption fee, we anticipate that these information requests will not be infrequent.

The requirement to provide funds, upon request, with the Taxpayer Identification Numbers ("TIN") of shareholders continues to pose problems for our members. As you know, the Commission's shareholder communication rules, i.e., Rules 14a-13, 14b-1, 14b-2, and 14c-1, require banks, savings institutions and brokers to obtain customer consent (non-objecting or consenting, depending on when the account was opened) to share certain customer information—name, address, securities position—with issuers. Banks and broker-dealers obtain customer consent or objection on a per account basis, not on a per security or type of security basis. Many of our members have reported to us that the vast majority of their customers have objected to release of this information to issuers of any securities held in their account. Indeed, one member has reported to us that 96% of its customer base had objected to release of this information.

The potential for conflict between the requirement in new Rule 22c-2 to provide mutual funds with TIN numbers for shareholders and customers' instructions not to divulge this information to issuers is high. Banks, savings institutions and broker-dealers that choose to comply with the redemption fee rule will be put in the unenviable position of having to contradict their customers' direction, a direction that was required to be obtained by Commission rules, and release non-public personal customer information to

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[2] FDIC December 2004 call report data.

[3] We recognize that Rule 22c-2 does not apply to money market funds, ETFs, and funds that affirmatively permit market timing.

any requesting mutual fund. Alternatively, these same financial intermediaries could ignore new Rule 22c-2 and the contract that they have signed with the various mutual funds in order to comply with customers' instructions obtained pursuant to the Commission's shareholder communication rules. At worse, financial intermediaries will be put in the position of determining which rules to comply with and which to ignore or violate. At best, financial intermediaries will find themselves in the middle of a customer relations disaster.

Customers of financial intermediaries, particularly the 40 million plus fiduciary and custody customers, are extremely guarded about their personal information becoming public. This point was reinforced most recently when banks and savings associations were required to gather certain personal information from their customers under authority of rules implementing the customer identification procedure requirements of Section 326 of the USA Patriot Act. We would anticipate that these same customers will raise similar concerns about personal information being released to mutual fund issuers despite their prior instructions to the contrary. Moreover, customers may very well be less understanding of the need to divulge personal, private information under Commission Rule 22c-2 than they were of the need for such information under the USA Patriot Act

To help mitigate these customer relations issues, the ABA strongly believes that the Commission should provide guidance on this matter. Perhaps the Commission could give some sort of direction to banks, savings associations and broker-dealers that can be referenced in alerting customers to the need, on occasion and where warranted, to provide requesting mutual funds with personal customer information. And, while we appreciate the Commission's statement in a footnote to the narrative section of the release adopting Rule 22c-2 to the effect that the Commission's privacy rule prevents a fund that receives shareholder transaction information from using the information for its own marketing purposes, unless permitted under the intermediary's privacy policies, that statement was more of an aside. A stronger statement regarding Commission privacy rules with an equally strong assurance of enforcement actions for any infractions of those rules will help financial intermediaries to give appropriate assurances to customers regarding the need to divulge, on occasion, personal financial information.

Need for Uniformity

The Commission has requested comment on whether it should establish uniform standards for redemption fees charged under the rule. Many of our members have previously expressed frustration regarding the lack of uniformity in the redemption fee area. A survey of mutual fund redemption fee practices in place <u>before</u> the Commission adopted Rule 22c-2 indicated that many mutual funds were assessing redemption fees of anywhere from .5% to 2% on purchases and redemptions that occurred within five business days to 360 calendar days. In addition to the wide variation in the amount of the fee assessed and the length of holding period for which the fee would be assessed, many transactions that one would not normally consider to be market timing were impacted by funds' redemption fee practices, including automated portfolio rebalancings that occur on a quarterly basis, exchanges within a plan's investment menu, changes brought on by the plan sponsor's decision to change investment options, plan loan transactions, and termination distributions. It is not uncommon for bank trust departments to handle transactions for over 200 funds on a daily basis. With each fund having the ability to set its own fee, holding period and other conditions, banks were experiencing a tremendous burden for monitoring fund transactions.

We do not see that situation changing under new Rule 22c-2. Funds are free to assess a redemption fee lower than 2%. In addition, funds are free to define the time period in which a redemption fee may be assessed on a purchases and redemptions so long as the time period is seven calendar days or more. Finally, funds are not required to exempt employee benefit transactions that were either not initiated by the participant-investor or where the participant has no control over the timing of the transaction. Lack of uniformity increases systems and compliance costs. Consequently, the ABA would strongly support the imposition of uniform standards with respect to mutual fund redemption fees.

The need for uniformity is most strong with respect employee benefit transactions. Some funds have chosen to exempt certain employee benefit transactions, while others have determined that all such transactions, regardless of whether the employee benefit plan participant initiated the transaction, are subject to redemption fees. The variations in the fund redemption fee policies with respect to employee benefit plan transactions increase substantially compliance costs and burdens. Those costs and burdens can be reduced significantly if the Commission were to require those funds that choose to assess redemption fees to exempt all employee benefit transactions where the employee does not control both the purchase and redemption of fund shares from the coverage of Rule 22c-2. Such an exemption would cover automated portfolio rebalancings that occur on a quarterly basis, exchanges within a plan's investment menu, changes brought on by the plan sponsor's decision to change investment options, plan loan transactions, and termination distributions. The exemption would not cover purchases and redemptions initiated by plan participants.

Exempting these employee benefit plan transactions will have added benefits. For example, assessing redemption fees in connection with plan loan transactions could very well raise issues under the Federal Reserve Board's Regulation Z. That regulation requires annual percentage rate ("APR") disclosures on loans, including participant plan loans. Assessment of a redemption fee may very well impact the calculation of the APR and its disclosure. If, however, plan loan transactions are exempted, there will be no need to consider whether Regulation Z APR disclosures need to be revised.

The Commission is also considering requiring that redemption fees not be charged if the amount of the fee would be fifty dollars or less. Under such a provision, a shareholder in a fund with a two percent redemption fee could redeem as much as 2,500 dollars of shares within seven days of purchasing them without paying a redemption fee. The ABA would strongly support a mandatory, uniform de minimis exception. Giving mutual funds the flexibility to determine whether a de minimis exception is appropriate, as the current rule does, forces banks and other intermediaries to incur significant systems and compliance costs.

We would also support a uniform fee waiver in the case of an unanticipated financial emergency. In this connection, we would renew our request that the Commission conform its definition of an unforeseeable emergency to the standards for hardship withdrawals set by the Internal Revenue Service for 401(k) plans. Because intermediaries that service retirement plans have a long history with the IRS' hardship withdrawal standards, uniformity in this regard would also reduce associated regulatory compliance costs.

The ABA supports the mandatory use of the FIFO accounting method, i.e., treating the shares held the longest time as being redeemed first, and shares held the shortest time as being redeemed last, to determine the amount of any redemption fee to be

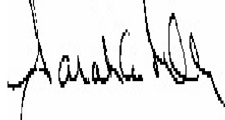
assessed. We believe that the FIFO method more precisely targets market timers, as opposed to frequent traders. This is true because the FIFO method would only trigger redemption fees when large portions of an account are rapidly purchased and redeemed, which as the Commission has previously noted, is a characteristic of abusive market timing transactions, but not when small portions of an account held over a longer period are redeemed.

Our members have indicated that there is less need for uniformity with respect to the amount of the redemption fee and the length of the holding period than with respect to the items discussed above. This is so because the systems employed by fund intermediaries can more easily handle variations in the amount of the fee and the holding period than variations in terms of exceptions, fee waivers and share accounting. If, as the Commission maintains, the redemption fee is a cost recovery fee, than uniformity with respect to the actual redemption fee assessed should not be required. We do not, however, believe there is a similar impediment to requiring a uniform holding period to which many of our members would not be opposed.

Conclusion

The ABA appreciates the opportunity to offer our comments on Rule 22c-2. If you have any questions or comments with respect to the issues raised in this letter, please Do not hesitate to contact the undersigned.

Sincerely yours,



Sarah A. Miller

cc: Robert Plaze
C. Hunter Jones
William C. Middlebrooks, Jr.