AMERICAN BENEFITS COUNCIL

VIA EMAIL
rule-comments@sec.gov

May 9, 2005

Jonathan G. Katz
Secretary
Securities and Exchange Commission
450 Fifth Street, NW
Washington, DC 20549-0609

Re: Comment letter on mutual fund redemption fees; File No. S7-11-04.

Dear Mr. Katz:

The American Benefits Council (the Council) appreciates the opportunity to provide comments on the need for uniform standards to eliminate administrative complexity, reduce costs, and ensure that millions of qualified retirement plan participants understand the rules when a fund chooses to impose a redemption fee under the Securities and Exchange Commission's (Commission's) final rule on mutual fund redemption fees.

The Council is a public policy organization representing principally Fortune 500 companies and other organizations that assist employers of all sizes in providing benefits to employees. Collectively, the Council's members either sponsor directly or provide services to retirement and health plans that cover more than 100 million Americans. Accordingly, we are keenly interested in this issue, not only from the perspective of the firms that provide retirement plan investment products and services, but rather, primarily from the perspective of companies that sponsor retirement programs on behalf of their employees and retirees.

The Council commends the Commission for its efforts to protect mutual fund investors and to restore investor confidence in mutual funds while at the same time making efforts to protect the interests of retirement plan participants and others who trade mutual funds through intermediaries. This latter concern is evidenced by the Commission's request for further comments on whether the Commission should set uniform standards for funds that choose to impose a redemption fee.

The Council strongly encourages the Commission to provide uniform standards for funds that choose to impose a redemption fee. As we stated in our comment letter dated May 10, 2004, retirement plans (in particular) need uniformity in order to reduce the costs of implementation, insure consistency of administration, and communicate the changes to affected participants.

The Council recommends that the uniform standards cover, at a minimum, (1) the types of transactions to which the fee will be applied, (2) use of the first-in, first-out (FIFO) method of calculating applicable fees, (3) mandating a de minimis waiver, (4) eliminating the financial emergency exception, (5) mandating the method used for imposing the fees or allowing the intermediary to choose, (6) providing a standardized format that will be used to provide requested information on participant trades to fund companies, and (7) requiring that funds not use information provided to them under this rule for marketing purposes (regardless of whether the intermediary has a privacy policy that covers the issue).

<u>Participant-Initiated Transactions</u>

While one Council member, a major fund manager, has indicated to the Council that it has made a determination that a broad imposition policy is in the best interests of its fund investors other Council members feel differently. This Council member's determination regarding the broad imposition policy is based in part on the conclusion that such a policy is easier to explain and therefore more easily understood by plan participants. It also allows them to address the increased costs that are borne by investors when there is short-term trading by any investor for any purpose and avoids the problem of defining which transactions should be excepted from the fee. Other Council members feel that the application of any redemption fee to retirement plan transactions should be limited to participant-initiated exchanges and interfund transfers.

Many Council members encourage the Commission to limit application of any redemption fees applied to retirement plan transactions only to participant-initiated exchanges and inter-fund transfers. Substantial differences in the types of transactions for which the fees will be applied between the various funds within a retirement plan will not only be difficult and costly to administer, it will be difficult to explain to plan participants. Council members are concerned that redemption fees will be imposed where it is clear that market timing is not the motivation for the activity and/or when the participant clearly does not control the timing of a particular transaction (such as loans, qualified domestic relations orders (QDROs) and distributions upon death or retirement). All of these transactions are subject to very detailed rules under the Internal Revenue Code and the Employee Retirement Income Security Act (ERISA) that control the timing of transactions and impose substantial penalties if the rules are broken. They do not lend themselves to potential market-timing abuses.

Council members believe that this exception is still needed even if the Commission provides for FIFO accounting and a de minimis exception (see discussion of these below). The Commission's rule specifically requested comments on this question and these Council members believe the answer is a resounding "yes". Without the exception, a participant who changes his or her investments shortly before a loan is processed could get hit with a redemption fee of up to $1,000 on a $50,000 loan. Under plan rules, the participant does not control the timing of the processing (and funding by selling investments) of his or her loan and often does not know the timing. Changing investments shortly before a QDRO is presented to the plan illustrates another situation, outside the control of the participant, that could result in the imposition of redemption fees in excess of $1,000.

Many retirement plan transactions are made for specific reasons that can be easily identified and monitored. These Council members encourage the Commission to limit redemption fee application to retirement plans so that only participant-initiated exchanges and transfers are covered. This would exclude the following retirement plan transactions from the redemption fees:

- Transactions that occur because the participant or his/her former spouse exercises a plan right or the plan's fiduciary makes a decision that results in the transaction (nonparticipant-directed). These include, among others, in-service withdrawals including hardship withdrawals, loans, payments required by QDROs, conversions between recordkeepers, assessment of plan expenses against the participant's account, and the plan sponsor changing the fund selections.
- Transactions that fall outside the definition of "discretionary transactions" as defined in Rule 16b-3 of the Securities Exchange Act of 1934. These transactions include employee and employer contributions into the plan (including elective deferrals and rollover contributions); trust-to-trust transfers; legally required or permitted corrective distributions including those made under the Internal Revenue Service EPCRS program; loan repayments and loan payoffs; distributions made on account of death, termination of employment, disability or retirement (even if there is a time delay after the event before the distribution); required minimum distributions and reinvestment of dividends.
- Automatic rebalancing where elected by the participant to occur on a pre-scheduled, recurring basis.

<u>FIFO</u>

The Council encourages the Commission to adopt the proposed provision that would require funds to determine the amount of any redemption fee by using the FIFO method. As noted by the Commission, this is the method commonly employed by funds that currently charge redemption fees and makes it less likely that the fee will be imposed on ordinary participant transactions such as employee deferrals followed by a rebalancing.

De Minimis Waiver

Under the proposed rule, the de minimis waiver would allow funds that impose a redemption fee to choose to forgo the assessment of the redemption fee if the value of shares redeemed is $2,500 or less (resulting in a fee of $50 or less). The Council believes administration would be greatly simplified, reducing costs and confusion, if any de minimis waiver is mandatory rather than optional for the funds. In addition, the Council suggests that the Commission consider raising the de minimis limit to fees of $200 or less (redemption of $10,000 or less). Market timers are unlikely to trade in small dollar amounts.

Financial Emergency

The Council recommends that the Commission eliminate the unanticipated financial emergency exception. Increasing the de minimis waiver amount would address many of these situations and the financial emergency exception will be exceedingly difficult for retirement plan administrators to process and communicate to participants. If a financial emergency exception is permitted, it should be mandatory to facilitate administration but again, the Council recommends simply eliminating the exception.

Many retirement plans already permit "hardship distributions" as defined and governed by ERISA. A new financial emergency exception with different requirements would cause confusion for participants. Even if the unanticipated emergency exception is defined exactly the same as a hardship distribution (with exactly the same documentation requirements), problems remain. For example, many plans permit distributions for any reason after a participant attains age 59-1/2 (as permitted under the Internal Revenue Code) and many of those plans do not permit hardship distributions after that age because participants have relatively liberal access to their accounts. Applying the hardship standards to these post-59-1/2 withdrawals would add an extra level of administrative complexity.

Methods to Impose the Fee

The Commission's proposed rule would have allowed mutual funds and third party intermediaries to impose the redemption fee on the underlying investor by one of three methods and the Commission's final rule asked for comments on whether the Commission should retain all three options and, if so, which entity should determine the option used to assess redemption fees. The three choices include requiring the intermediary (1) to transmit at the time of each transaction the account number used by the intermediary to identify the transaction, (2) to identify redemptions that would trigger the application of the redemption fee and transmit holdings and transaction information to the fund sufficient to allow the fund to impose the fee, or (3) to impose the redemption fee and remit the proceeds to the fund.

The Council recommends that the Commission mandate the third option of having the intermediary impost the redemption fee and remit the proceeds to the fund. As the Commission pointed out, this method is the most cost-effective for most parties. If the Commission determines that it should allow other choices because small intermediaries may not have the capability to collect and transmit redemption fees, clearly the intermediaries should be given the choice. It would be even more difficult for the small intermediary to deal with two or three methods if the choice is left up to the funds.

Any method should include an error correction process, and this is especially important if the intermediary imposes the fees. Funds should refund fees collected in error with reasonable documentation of the error.

<u>Standardized Format for Information</u>

The final regulations now require that intermediaries provide certain information upon the request of the funds. The Council commends the Commission for taking this common sense approach instead of mandating that volumes of information be passed from intermediaries to funds on a regular basis. However, the Council also recommends that the Commission provide a standardized format for providing the information to the funds when it is requested. Without such standardization, different fund families may request information in various formats, resulting in additional costs and administrative issues for intermediaries.

<u>Not Used for Marketing</u>

The Council also recommends that the Commission specifically preclude the use of information attained by the funds under the requirements of the regulation for marketing or other purposes unrelated to the imposition of redemption fees. Intermediaries will be required to provide information on their customers to the fund companies and are understandably concerned about what might be done with that information. Although the final regulation states that the fund cannot use the information for its own marketing purposes unless it is permitted under the intermediary’s privacy policies, this prohibition does not go far enough. The direction should not be tied to a policy that may not exist or may not be broad enough and should not be limited to marketing activities.

<u>Costs</u>

Finally, the Council believes that the estimates of the costs of implementation contained in the final regulations are extremely low. One of the Council's members estimated their cost of implementation would be $6 to $7 million alone even if many of the requirements are made uniform. The more flexibility allowed, the higher the estimated costs.

Many of the retirement plan administrator's business, operations and systems will need to be reviewed and modified to handle the imposition of redemption fees. Listed below are some of the areas of substantial cost:

- Contracts with both fund families and plan sponsors must be renegotiated to allow (1) for the imposition of redemption fees on individual participants and (2) retirement plan administrators to provide confidential information on participants to the mutual funds.
- Reprogramming of recordkeeping systems will be necessary to allow, among other things, measurement of holding periods, imposition of fees and production of reports necessary for information requested by the mutual fund companies.
- Participants typically direct their investments under the plan through web sites, telephonic voice response systems or call center personnel. The websites and voice response systems will need to be reprogrammed to notify participants of redemption fees and calculate and communicate redemption fee estimates. Call center personnel will need to be retrained to answer questions from participants regarding redemption fees and will need reprogrammed systems to access the necessary information.
- All retirement plan documents, including, but not limited to, plan documents, summary plan descriptions and plan administration materials will need to be reviewed, rewritten and reprinted to include the needed changes.
- Significant time, money and energy will be expended to explain these changes to participants through written communication and/or in-person meetings.

We appreciate the opportunity to provide further input in the development of potential rules in this area, and to comment on such rules. We believe that the American Benefits Council brings an important and unique perspective of the employer sponsors of retirement plans and we would be pleased to make this information and perspective available to the Commission. If additional information from us would be helpful, please call me at 202-289-6700.

Sincerely,

Jan M. Jacobson

Director, Retirement Policy