

MEMO# 7864

May 14, 1996

ADDITIONAL SEC INTERPRETIVE RELEASE AND FINAL RULES ON USE OF ELECTRONIC MEDIA TO DELIVER INFORMATION

1 Release No. IC-21945; IA-1562 (May 9, 1996). 2 See Memorandum to Accounting/Treasurers Committee No. 47-95, Closed-End Fund Committee No. 34-95, SEC Rules Committee No. 73-95, Unit Investment Trust Members No. 52-95, dated October 10, 1995. 3 Release No. IC-21946 (May 9, 1996). Both the interpretive release and the final rules are available at the SEC's World Wide Web address: <http://www.sec.gov/>. May 14, 1996
TO: SEC RULES COMMITTEE No. 40-96 CLOSED-END FUND COMMITTEE No. 13-96 UNIT INVESTMENT TRUST COMMITTEE No. 22-96 INVESTMENT ADVISERS COMMITTEE No. 9-96 SUBCOMMITTEE ON ADVERTISING No. 7-96 BROKER/DEALER ADVISORY COMMITTEE No. 8-96 TRANSFER AGENT ADVISORY COMMITTEE No. 26-96 RE: ADDITIONAL SEC INTERPRETIVE RELEASE AND FINAL RULES ON USE OF ELECTRONIC MEDIA TO DELIVER INFORMATION

The Securities and Exchange Commission has issued an interpretive release that provides broker-dealers, investment advisers and transfer agents with guidance in using various types of electronic media to satisfy their information delivery requirements under the Securities Exchange Act of 1934 and the Investment Advisers Act of 1940.¹ The release also provides several additional examples for investment companies that respond to comments from the Institute and others on an interpretive release on electronic media issued by the SEC in October 1995 (the "October Release").² In addition to the interpretive release, the SEC has issued final rule amendments that codify some of the interpretations set forth in the October Release.³ The interpretive release and the final rule amendments are summarized below. The interpretative release will be effective on the date of its publication in the Federal Register. The SEC seeks comment on the issues discussed in the release no later than 45 days after publication of the release in the Federal Register. If you have any comments that you would like the Institute to consider including in a comment letter, please contact the undersigned by telephone (at 202/326-5923) or electronic mail (at gavis@ici.com) by Friday, June 7, 1996. 2I. Interpretive Guidance for Broker-Dealers, Investment Advisers and Transfer Agents A. General The interpretive release is intended to provide broker-dealers, investment advisers and transfer agents with guidance on how they may electronically deliver information to clients and customers. Although it does not specify the electronic medium that broker-dealers, investment advisers or transfer agents may use, it does provide a list of those rules under which they may provide documents electronically (see pages 18-25). Of particular note, the release allows for the electronic delivery of

confirmation statements under Rule 10b-10 of the Exchange Act, as the Institute had recommended. The release generally applies the same basic principles that were articulated in the October Release. First, broker-dealers, investment advisers and transfer agents should consider the extent to which electronic communication provides timely and adequate notice that such information is available electronically. Second, the release indicates that persons to whom information is sent electronically should be given access to information that is comparable to that which would have been provided if the information were delivered in paper form. Third, if electronic delivery is used by broker-dealers, investment advisers or transfer agents, they should have reason to believe that the electronically delivered information was actually received by the intended recipients. According to the release, this can be achieved by (1) obtaining the intended recipient's informed consent to electronic delivery, and assuring that he or she has appropriate access and notice; (2) obtaining actual evidence of receipt through a return receipt electronic mail message; or (3) disseminating information through certain facsimile methods.

B. Personal and Financial Information and Other Communications The release indicates that, with respect to certain information that is specific to a particular person's "personal financial matters" (e.g., confirmation statements), broker-dealers, investment advisers and transfer agents "should take reasonable precautions to ensure the integrity, confidentiality and security of that information, regardless of whether it is delivered through electronic means or in paper form." In addition, the release requires that, before personal financial information can be transmitted electronically, an informed consent be obtained from the investor. The release also indicates that various communications that are required under the Exchange Act or the Investment Advisers Act to be received by broker-dealers or investment advisers from customers or clients (e.g., consents to a transaction or acknowledgement of receipt of certain disclosures) may be communicated electronically to the broker-dealers or investment advisers. The electronic delivery of non-required information that, in some cases, is provided voluntarily to customers and clients is not covered by the release and therefore does not have to comply with it. In this regard, the release states that it is permissible for investment advisers to use various electronic media to disseminate advertisements for their services. The release notes, however, that, if an adviser uses a publicly available electronic medium such as a World Wide Web site to provide information about its services, the adviser would not qualify for the exemption from registration in Section 203(b)(3) of the Advisers Act. Finally, the release does not directly address issues related to electronic mail. It indicates that self-regulatory organization rules concerning the supervisory requirements for electronic communications should be based on the content and audience of the message, and not merely the electronic form of the communication, and suggests that the self-regulatory organizations should provide guidance in this area.

II. Additional Examples for Investment Companies The October Release contained a series of examples that illustrated the general concepts set forth in the release. The attached interpretive release contains additional examples, several of which relate directly to mutual funds, based on questions that were raised by the Institute and other commenters. One follow-up example responds to the Institute's request for clarification concerning the use of electronic prospectuses and supplemental sales literature. According to the example, a fund may not provide a hyperlink from electronic supplemental sales literature to an electronic prospectus, if the prospectus cannot be viewed by an investor on-line. The release notes that "[a]s technology develops, some users may have the capacity to download and view a prospectus in no more time than it takes to jump via hyperlink from the sales literature to the prospectus . . . [and u]nder those circumstances, the capacity to download would be considered to give those users reasonably comparable access to the prospectus that would provide sufficient access." (See Example 5, p.27). The release also provides a follow-up example that responds favorably to

the Institute's recommendation that mutual funds be allowed to use quarterly account statements or quarterly newsletters to provide investors who have consented to electronic delivery with notification of prospectus amendments, including both routine and material amendments. (See Example 5, p.27). The release also responds affirmatively to the Institute's request for clarification that if a fund's on-line prospectus has the same text as the paper version, but the text appears in different format, the fund does not have to make a separate filing under Securities Act Rule 497. (See Example 6, p.28). Finally, at the Institute's recommendation, an example clarifies that, if a mutual fund produces an electronic version of a prospectus that contains, for example, a movie, the fund does not have to provide a written transcript of the movie to those investors who are provided with the paper version of the prospectus. The example notes, however, that the fund may either file both versions of the prospectus with the Commission as part of the fund's registration statement or file a written transcript of the movie in an appendix to the paper version, and that each version of the prospectus should indicate that there may be other versions of the prospectus available. (See Example 7, p.28).

III. Final Rule Amendments

The SEC also issued final rule amendments that make technical changes to certain SEC rules and forms to address use of electronic media by issuers. The SEC's rules that prescribe the physical appearance of a paper document are amended to provide that an issuer, when delivering an electronic document, may comply with the requirements by presenting the information in a format readily communicated to investors. In addition, as recommended by the Institute, the SEC did not adopt the rule proposal that would have required that, if material graphic, image and audio information is included in one version of a disclosure document, but not in other versions, the issuer must include in the other versions a fair and accurate description or transcript of the omitted information. The SEC has amended Rule 304 of Regulation S-T to provide that whenever a document delivered to investors or others includes graphic, image or audio information that cannot be reproduced in an EDGAR filing, the EDGAR filing must include a fair and accurate narrative description, tabular presentation or transcript of the omitted material. Finally, the rule amendments require that prospectuses disseminated electronically by investment companies include a statement on their cover page that the SEC maintains a Web site that contains the Statement of Additional Information, material incorporated by reference and other information.

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