

MEMO# 17401

April 19, 2004

DRAFT COMMENT LETTER ON MANDATORY REDEMPTION FEE PROPOSAL; CONFERENCE CALL ON APRIL 28

ACTION REQUESTED [17401] April 19, 2004 TO: BANK AND TRUST ADVISORY COMMITTEE No. 8-04 BROKER/DEALER ADVISORY COMMITTEE No. 13-04 OPERATIONS COMMITTEE No. 7-04 PENSION COMMITTEE No. 20-04 PENSION OPERATIONS ADVISORY COMMITTEE No. 32-04 SEC RULES COMMITTEE No. 36-04 SMALL FUNDS COMMITTEE No. 24-04 TAX COMMITTEE No. 13-04 TRANSFER AGENT ADVISORY COMMITTEE No. 36-04 RE: DRAFT COMMENT LETTER ON MANDATORY REDEMPTION FEE PROPOSAL; CONFERENCE CALL ON APRIL 28 As you know, the Securities and Exchange Commission recently proposed new Rule 22c-2 under the Investment Company Act, which would require mutual funds (with certain limited exceptions) to impose a two percent redemption fee on the redemption of shares purchased within the previous five days.¹ The Institute has prepared a draft comment letter on the proposal, which is attached and summarized below. Comments on the proposal must be filed with the SEC by Monday, May 10th. The Institute will hold a conference call on Wednesday, April 28, 2004 at 2:00 p.m. Eastern time to discuss the draft letter. The dial-in number for the call is 888- 425-4795 and the pass code is 11500. If you plan to participate on the call, please send an e-mail to Gail Robinson at grobinso@ici.org. If you are unable to participate on the call, please provide me your comments before the call, if possible, by phone (202-371-5430), fax (202-326- 5841), or email (rcg@ici.org). The draft comment letter notes that the Institute continues to support the adoption of a rule that requires funds to impose a redemption fee, and therefore supports the objectives of the 1 See Memorandum to Bank and Trust Advisory Committee No. 5-04; Broker/Dealer Advisory Committee No. 8-04; Operations Committee No. 4-04; Pension Committee No. 12-04; Pension Operations Advisory Committee No. 22-04; SEC Rules Committee No. 22-04; Small Funds Committee No. 17-04; Tax Committee No. 9-04; and Transfer Agent Advisory Committee No. 25-04 [17171], dated March 8, 2004. 2 proposed rule in the comment letter. The letter recommends a number of modifications to the proposed rule, however, to ensure that it achieves its objectives in the most efficient way possible. In summary, the Institute's principal comments on the proposal are as follows: • We recommend several modifications to the proposed rule to clarify its application to funds that sell shares through intermediaries (e.g., broker-dealers), retirement plans, 529 plans, funds of funds, master-feeder structures, and insurance company separate accounts; • We recommend that the final rule establish two percent as a minimum level for redemption fees and allow the imposition of a higher redemption fee if a fund's board makes certain findings; • We recommend that the final rule require a LIFO accounting method for determining which

transactions are subject to the fee, rather than FIFO as proposed; • We recommend that the final rule not include an exception for unanticipated financial emergencies because such an exception is largely unnecessary and would be highly susceptible to abuse; • We recommend that the final rule include a mandatory de minimis exception for redemptions that would trigger a fee of \$100 or less, rather than a discretionary de minimis exception for redemptions that would trigger a fee of \$50 or less as proposed; • We recommend that the exception for funds designed for active trading allow such funds the option of adopting a non-fundamental policy (as long as they also provide investors with notice of any change to that policy), rather than requiring them to adopt a fundamental policy as proposed; and • We recommend that intermediaries be required to provide funds with transactional information upon request, rather than being required to provide a complete set of transaction information at least weekly as proposed. We would welcome comment on all aspects of the draft letter. There are several issues that we would particularly like to highlight, some of which may not be reflected in the draft letter: 1. Should the letter recommend that there be some implementation period before which the imposition of redemption fees becomes mandatory? If so, what should that period be? 2. As noted above, the draft letter recommends that funds be permitted to impose redemption fees higher than two percent. To give the SEC greater assurances that funds would not utilize that flexibility unreasonably, should the letter suggest an upper limit for redemption fees covered by the rule? If so, how high should that limit be? 3. The draft letter states that there would be implementation costs with both LIFO and FIFO. Which would be more expensive to implement - LIFO or FIFO? 4. The draft letter points out a potential conflict between the NASD's CDSC rule and a strict LIFO or FIFO rule for redemption fees. Should shares subject to a CDSC simply be exempt from the scope of Rule 22c-2? 5. The Proposing Release invites general comments on the topic of fair value pricing. Except for footnote 3, the letter does not currently address this topic. Are there aspects of fair value pricing that you would like us to raise in this comment letter? Robert C. Grohowski Associate Counsel Attachment (in .pdf format)