The Asset Management Industry
SERVING INDIVIDUAL INVESTORS
INVESTMENT COMPANY INSTITUTE

COMMENT LETTER

May 28, 1999

Comment Letter on SEC Proposed Rules Re Canadians' Retirement Accounts, June 1999

May 28, 1999

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

Re: File No. S7-10-99

Dear Mr. Katz:

The Investment Company Institute1 appreciates the opportunity to comment on the Commission's proposal to create new Rules 237 under the Securities Act of 1933 (the "1933 Act") and 7d-2 under the Investment Company Act of 1940 (the "1940 Act") and to amend Rule 12g3-2 under the Securities Exchange Act of 1934 (the "Exchange Act"). 2 The Commission's proposal would permit foreign securities, including foreign investment company securities, to be offered and sold to US participants in certain Canadian tax-deferred retirement accounts without the securities being subject to registration, and without the investment company being subject to registration, under our federal securities laws. This would allow Canadians who reside in the United States to effect transactions in their Canadian retirement accounts, including the purchase of investment company shares, without running afoul of US law. The Institute's comments focus primarily on the Commission's proposal to provide relief under Section 7(d) of the 1940 Act to permit Canadian mutual funds to offer and sell their securities to those Canadian investors without compliance with the 1940 Act.

The Institute is sympathetic to the concerns of Canadians now residing in the US who are unable to continue to actively manage their Canadian tax-advantaged retirement accounts.3 Accordingly, the Institute has no objection to granting relief to these investors, so long as any relief under Section 7(d) of the 1940 Act is appropriately limited and the Commission retains the ability to monitor compliance with the rule. The Institute is pleased that the limitations contained in proposed Rule 7d-2 appear to satisfy this standard, although we do recommend that two additional requirements be added to strengthen the SEC's ability to monitor compliance with the rule.

It should be noted that US citizens resident in Canada face similar constraints under Canadian securities laws. In particular, US investors who reside in Canada and have interests in US tax-advantaged retirement accounts, such as IRAs and 401(k) accounts, are unable to actively manage these US retirement accounts. In October 1997, Canadian Securities Administrators issued a proposed National Instrument that would provide an exemption from the broker-dealer registration and prospectus delivery requirements to permit broker-dealers and their agents to trade in non-Canadian securities, including US mutual funds, with US citizens resident in Canada with respect to their tax-advantaged retirement savings plans.4 We understand that adoption of this National Instrument has been delayed pending Commission consideration of the matters covered in the Commission's rule proposals. In light of the Commission's proposal, we believe the SEC should now urge the Canadian Securities Administrators to go forward with adoption of the National Instrument in order to provide comparable, reciprocal relief for US citizens, broker-dealers, and issuers.

The Institute's comment letter is in two parts. The first part discusses our support for the limitations in proposed Rule 7d-2 and our recommendations to enhance the SEC's ability to monitor compliance with them. The second part sets forth technical comments on the proposed rules.

Any exemption from Section 7(d) of the 1940 Act should be narrowly drawn and allow the Commission to continue effectively to protect investors in the US.

Section 7(d) of the 1940 Act represents a prudential standard that ensures that investors in the US receive the same essential investor protections whether they acquire shares in a foreign fund or a US-based fund. Permitting foreign funds to offer their shares in the US without requiring that they comply with the 1940 Act would unfairly penalize US funds that must comply with the Act and would put at risk the broad public confidence enjoyed by the US fund industry. Accordingly, any exemptions from the requirements of Section 7(d) should be narrowly drawn and contain appropriate safeguards to assure the protection of US investors.

We are pleased that the conditions included in proposed Rule 7d-2 appear to address these concerns. Among other things, the rule would apply only to transactions in participant-directed tax-advantaged Canadian retirement accounts made in accordance with Canadian law. This means, among other things, that the relief provided by the rule generally would be limited to transactions in connection with an exchange or reallocation of existing Canadian retirement account investments. While the rule would permit transactions in connection with new investments made with additional contributions, we understand that most Canadians who relocate to the US would no longer be residents of Canada for tax purposes and thus would not be able to contribute significant additional income to their Canadian retirement accounts.

The proposal would impose other investor protection safeguards also. Securities offered and sold in the US in reliance on the rule would have to include prominent disclosure that they are not registered in the US. In addition, the rule would apply only to transactions initiated by Canadian retirement plan participants or their authorized agents, would limit activities in which persons relying on the rule could engage and would preserve the applicability of the anti-fraud provisions of US securities laws to the transactions. The

proposal also would not permit persons relying on the rule to disclaim the applicability of Canadian law or jurisdiction in transactions under the rule. The Institute supports all of these conditions.

The Commission requested comment on whether to require certain additional conditions. We believe that two of these conditions should be added to Rule 7d-2 to provide the Commission with adequate tools to monitor compliance with the rule's conditions and to take appropriate action in the event of any abuses.5

First, we recommend that persons relying on the rule be required to file a form with the Commission designating an agent for service of process in the US.6 The designation of an agent for service of process will facilitate the ability of the Commission or Canadian retirement account participants to obtain service in the US in the event legal action relating to transactions under the rule is warranted.

Second, we recommend that the proposed rules include a requirement that any person relying on the rules provide the Commission, upon request, with information, documents, testimony and assistance relating to any offers or sales made in reliance on the rules. This requirement, which we do not believe would be unduly burdensome, will better enable the Commission to ensure compliance with the requirements of the rule and will facilitate the Commission's ability to investigate allegations of fraud.7

Technical Comments

The Institute has the following technical comments on the proposals.

a) Rule 237(a)(3)(i) and Rule 7d-2(a)(3)(i) define an eligible security, in part as a security that "is offered to a Participant, or sold to his or her Canadian Retirement Account..." The Institute is concerned that this language might permit the offer of securities to a person who owns a Canadian retirement account even if the securities will not be held in the Participant's retirement account. For this reason, Rule 237(a)(3)(i) and (b)(2) and Rule 7d-2(a)(3)(i) and (b) should be revised in relevant parts to read: "...is offered to a Participant for his or her Canadian Retirement Account, or sold to his or her Canadian Retirement Account..." Rule 237(b)(1)(i) and Rule 7d-2(b)(1)(i) should be revised to read: "Processing requests for a Participant (or his or her authorized agent) for the purchase, sale, exchange, or redemption of an Eligible Security in the Participant's Canadian Retirement Account, and effecting other routine transactions under Canadian law in or for such account;".

b) The Institute recommends that Subdivision (b)(1)(iv) of proposed Rule 237 and 7d-2 be revised to read: "Delivering updated written offering materials, shareholder reports, account statements, proxy statements, or other materials concerning Eligible Securities of a Qualified Company held in a Canadian Retirement Account." The reason for this revision is as follows. As defined in the Rules, "Qualified Company" would mean an issuer whose securities are qualified for investment on a tax-deferred basis in a Canadian Retirement Account. Under this definition, however, it is not necessary for the particular securities sold to the Participant to be a qualified for tax-deferred treatment. The term "Eligible Security" would mean a security issued by a "Qualified Company" that is offered to the Participant or sold to his or her Canadian Retirement Account in reliance on the Commission's proposed rules.

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The Institute appreciates the opportunity to comment on the Commission's proposals to facilitate the ability of Canadians who are resident in the US to actively manage their Canadian retirement accounts.

Sincerely,

Craig S. Tyle

cc: Paul Roye, Director
Division of Investment Management

Robert E. Plaze, Associate Director
Division of Investment Management

ENDNOTES

1 The Investment Company Institute is the national association of the US investment company industry. Its membership includes 7,546 open-end investment companies ("mutual funds"), 457 closed-end investment companies and 8 sponsors of unit investment trusts. Its mutual fund members have assets of about $5.730 trillion, accounting for approximately 95% of total industry assets, and have over 73 million individual shareholders.

2 Release Nos. 33-7656, 34-41189, IC-23745 (March 19, 1999) (the "Release").

3 We note that the problems Canadians residing in the US face in managing their tax-advantaged Canadian retirement accounts would be ameliorated if Canadian law is amended to provide Canadian retirement account participants greater flexibility to invest in foreign securities. As a general matter, the Institute supports the elimination of "foreign content" restrictions imposed on retirement plans under the laws of many foreign countries. Removing these restrictions can contribute importantly both to improved investment return and the protection of retirement funds through diversification. See "Selected Issues in International Taxation of Retirement Savings," Perspective, Volume 3, Number 4 (August, 1997), Investment Company Institute.

4 See, Notice of Proposed National Instrument 35-101 and Companion Policy 35-101CP Conditional Exemption from Registration for United States Broker-Dealers and Agents. October 17, 1997.

5 The Commission also requested comment on whether a person relying on Rule 237 or 7d-2 should be required to obtain from a Canadian retirement account participant a written acknowledgment that the securities offered or sold in reliance on these rules are not subject to the registration provisions of the US securities laws. Based upon the disclosure requirements of Subdivision (b)(2) of proposed Rules 237 and 7d-2, we do not believe a written acknowledgment is necessary.

6 The requirement to make a filing with the Commission designating an agent for service of process would not appear to be burdensome. We note that the rule petition filed with the Commission by the Investment Funds Institute of Canada in February 1998 contained a condition requiring a Canadian mutual fund relying on the rule to file a notification with the Commission.

7 The requirements to designate an agent for service of process and to provide the

Commission with information upon request would be comparable to conditions contained in proposed National Instrument 35-101.
