The
ERISA
Industry
Committee

SUBMISSION OF THE ERISA INDUSTRY COMMITTEE TO THE SECURITIES AND EXCHANGE COMMISSION

COMMENTS REGARDING REDEMPTION FEES IMPOSED BY MUTUAL FUNDS

<u>File No.: S7-11-04</u>

May 9, 2005

The ERISA Industry Committee ("ERIC")[1] is pleased to submit the following comments regarding the imposition of redemption fees by mutual funds. ERIC's comments, which are summarized on pages 5 - 6, below, respond to issues raised by the Commission in the adopting release accompanying new rule 22c-2 under the Investment Company Act.

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[1] ERIC is a nonprofit association committed to the advancement of the employee retirement, health, incentive, and compensation plans of America's major employers. ERIC's members provide comprehensive benefits to tens of millions of active and retired workers and their families and beneficiaries. ERIC's members' plans are the benchmarks against which industry, third-party providers, consultants, and policy makers measure the design and effectiveness of employee benefit, incentive, and compensation plans. ERIC's members are engaged daily with meeting the demands of both their enterprise and the needs of employees while dealing with an increasingly complex web of benefit and compensation laws. ERIC, therefore, is vitally concerned with proposals affecting its members' ability to provide employee benefits, incentive, and compensation plans, their costs and effectiveness, and the role of those plans in the American economy.

1400 L Street, N.W.
Suite 350
Washington, DC 20005
TEL: (202) 789-1400
FAX: (202) 789-1120
www.eric.org

Introduction

In general terms, rule 22c-2 allows registered mutual funds to impose a redemption fee of up to 2% on the redemption of mutual fund shares before the end of a specified period after the shares were purchased. Certain funds (such as money market funds) are not subject to the requirements of the rule unless they elect to impose a redemption fee. We disregard such “excepted funds” for purposes of this submission.

ERIC filed comments on the Commission’s proposed rule. The proposed rule would have required a mutual fund to impose a redemption fee of 2% of the amount redeemed on shares held for five business days or less. Rather than requiring each fund to impose a 2% redemption fee, the final rule requires the directors of a mutual fund either (1) to impose a redemption fee of up to 2% of the amount redeemed or (2) to determine that imposition of a redemption fee is either not necessary or not appropriate.

Any redemption fee would be retained by the mutual fund and would be imposed on shares redeemed within a period (of at least seven calendar days) that, in the judgment of the mutual fund’s board, is necessary or appropriate to recoup the costs that the fund may incur as a result of the redemptions or to otherwise eliminate or reduce any dilution of the value of the fund’s securities. The adopting release states that directors may impose the fee to offset the cost of short-term trading in fund shares and/or to discourage market timing and other short-term trading strategies.

Under the Commission’s proposed rule, mutual funds would have had to require financial intermediaries -- such as a retirement plan -- to provide them with weekly information about transactions effected by the beneficial owners of mutual fund shares in the intermediaries’ accounts. By contrast, the final rule generally requires a mutual fund to enter into an agreement with each of its financial intermediaries -- including the administrator or recordkeeper of a participant-directed individual account retirement plan -- under which the intermediary agrees (1) to provide, at the fund’s request, the taxpayer identification numbers of all those who purchased, redeemed, transferred, or exchanged shares held through an account with the intermediary and the amounts involved in, and dates of, such transactions and (2) to execute any instructions that the intermediary receives from the fund to restrict or prohibit future purchases or exchanges of fund shares by a party that the fund identifies as having engaged in transactions that violate fund policies. The final rule makes clear that the term “financial intermediary” means, in the case of a participant-directed employee benefit plan, a retirement plan’s administrator or any entity that maintains the plan’s participant records.

The adopting release requests comment on whether the Commission should establish a uniform redemption fee for those funds that impose such a fee and, if so, the terms of the fee. The adopting release suggests that a uniform fee might be less costly for intermediaries to collect and might make intermediaries more willing to collect the fees.

The adopting release was published in the Federal Register on March 18, 2005, and asked for comments by May 9, 2005. *See* 70 Fed. Reg. 13,327.

Background

All of ERIC's members sponsor individual account retirement plans, including some of the largest individual account plans in the country, covering tens of thousands of employees and beneficiaries. These plans, most of which are § 401(k) plans, commonly give participants the right to direct the investment of all or part of the funds in their accounts. These plans are extremely important to employers and employees alike. They provide valuable retirement and other benefits to employees and help employers to recruit, retain, and motivate employees. ERIC's members therefore have a vital interest in assuring that the rules achieve their objectives in a fashion that is consistent with sound plan design and administration.

In 1999, according to the U.S. Department of Labor, there were approximately 335,000 § 401(k)-type individual account plans, with over 38 million active participants and over $1.7 trillion in assets. The vast majority of these plans allow participants to direct the investment of all or part of the assets allocated to their accounts. Of the 335,000 § 401(k)-type individual account plans in 1999, over 269,000 were participant-directed plans, with over 33 million active participants and over $1.5 trillion in assets.[2] About one-third of all mutual fund shares are held by retirement plans.[3]

The § 401(k) plans sponsored by major employers typically offer participants and beneficiaries the opportunity to allocate their accounts among a number of different investment options, many of which are mutual funds sponsored by different mutual fund families. By offering a broad range of funds, sponsored by different mutual fund families and managed by different investment advisers, plans seek to implement the objectives of prudence and diversification reflected in the Employee Retirement Income Security Act of 1974 ("ERISA").[4]

A § 401(k) plan sponsored by a major employer typically engages in many thousands of transactions each month, including --

(a) accepting employee contributions, which are typically made by payroll deduction;

(b) accepting employer contributions, which are often made on a matching basis throughout the year, with the employer matching each employee's

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[2] Employee Benefits Security Administration, U.S. Dep't of Labor, Private Pension Plan Bulletin, Abstract of 1999 Form 5500 Annual Reports, Tables D6 & D7 (Summer 2004). The Employee Benefit Research Institute estimated that, by the end of 2003, the number of workers participating in § 401(k) plans had swelled to 42 million and that § 401(k) plan assets had grown to $1.9 trillion. *See* EBRI Issue Brief No. 272 at p.4 (Aug. 2004).

[3] 69 Fed. Reg. 11,764 n.17 (March 11, 2004).

[4] ERISA § 404(a)(1).

contribution based on a formula set forth in the plan (*e.g.*, a matching contribution of 50% of the employee's contribution);

(c) accepting rollover contributions that employees make from plans sponsored by their prior employers and from IRAs;

(d) distributing benefits to terminated and retired employees and their beneficiaries (some of which are made by direct rollover to another employer-sponsored plan or to an IRA);

(e) distributing benefits to employees who make withdrawals from their accounts because of hardship or other reasons before terminating employment;

(f) distributing loans to employees and receiving loan payments (generally by payroll deduction) from employees;

(g) receiving funds from other plans in the case of plan mergers and spin-offs from other plans;

(h) distributing funds to other plans in the case of plan mergers and spin-offs to other plans;

(i) making automatic investment transfers from one investment fund to another pursuant to plans' automatic rebalancing features; and

(j) making participant-directed investment transfers from one investment fund to another within the plan.

Of the ten transaction categories we have listed, **only one** -- participant-directed investment transfers -- is typically used to implement the short-term trading strategies that are the target of the redemption fees. For a variety of reasons, the transactions in the other categories do not lend themselves to short-term trading strategies. For example, the income tax consequences of distributions, withdrawals, and loans (including the 10% tax on early distributions[5]), and participants' lack of control over the timing of rollovers, plan transactions, and automatic rebalancing, generally make such transactions unsuitable vehicles for implementing short-term trading strategies. Likewise, when a participant elects to take a distribution, withdrawal, or loan from a plan, the participant generally cannot determine the fund or funds that are the source of the distribution, withdrawal, or loan; the identity of the fund or funds is determined by the terms of the plan and/or the plan's administrative procedures. Requiring a participant to pay a redemption fee for reasons that are beyond the participant's control would be both punitive and unproductive.

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[5] *See* Int. Rev. Code § 72(t).

Summary of Comments

1. The Commission should impose uniform share aging and tracking requirements for all purposes under rule 22c-2. Specifically, the Commission should provide that, for both reporting and redemption fee purposes, mutual funds and financial intermediaries that are participant-directed retirement plans must (i) use FIFO accounting and (ii) disregard all transactions by participant-directed individual account retirement plans other than participant-directed investment transfers. For example, in imposing a redemption fee, a fund should be required to disregard purchases and redemptions attributable to --

   (a) the plan's receipt of employee and employer contributions, rollovers, and loan payments,

   (b) distributions, withdrawals, rollovers, and loans from the plan,

   (c) plan mergers, spin-offs, and terminations and plan-to-plan transfers, and

   (d) automatic portfolio rebalancing.

   Likewise, the administrators and recordkeepers of participant-directed individual account retirement plans should be required to disregard such transactions for reporting purposes under rule 22c-2(a)(2)(i).

2. There will be no need for a "de minimis" rule or for waivers if the Commission adopts the recommendation in paragraph 1, above.

3. The Commission should not fix the rate at which a mutual fund must impose any redemption fee nor should the Commission specify the length of time that mutual fund shares must be held in order to avoid any redemption fee.

4. The Commission should amend rule 22c-2(a)(2)(i) to provide that an agreement between the fund (or its principal underwriter) and a retirement plan administrator or recordkeeper need not require the administrator or recordkeeper --

   (a) to respond to more than one request by the fund per month,

   (b) to furnish information that it has previously furnished to the fund, or

   (c) to furnish information relating to transactions that occurred more than 12 months before the date of the request.

5. The Commission should amend rule 22c-2(a)(2)(ii) to provide that an agreement between the fund (or its principal underwriter) and a retirement plan administrator or recordkeeper may, if the parties to the agreement so choose, impose reasonable restrictions on the instructions that the fund may issue, including --

   (a) a requirement that the fund's instructions be reasonable (for example, with respect to their effective date),

(b) restrictions designed to assure that the plan and its fiduciaries and administrators comply with applicable law (such as the applicable provisions of ERISA (including the regulations under ERISA § 404(c)) and the Internal Revenue Code),

(c) a requirement that the fund furnish to the plan administrator or recordkeeper a written explanation of the reason for its instruction,

(d) a provision that gives the plan administrator or recordkeeper an opportunity to verify the fund's explanation of the reason for its instruction, and

(e) a provision allowing any dispute between the fund and the plan administrator or recordkeeper regarding the fund's instructions to be submitted to an independent party for resolution pursuant to an alternative dispute resolution ("ADR") process.

6. The Commission should amend rule 22c-2(a)(2) to provide that a retirement plan administrator or recordkeeper may agree to furnish information to a fund, or to comply with the fund's instructions, in accordance with the rule only if the fund agrees to reimburse the administrator or recordkeeper for any additional expenses that the administrator or recordkeeper incurs in complying with the fund's request for information or the fund's instructions.

7. The Commission should expressly forbid a mutual fund from using, directly or indirectly, any information that a retirement plan administrator or recordkeeper furnishes to the fund in accordance with a rule 22c-2(a)(2) agreement for any purpose other than one of the purposes identified by the Commission:

(a) to monitor trading,

(b) to identify those who engage in frequent trading that is inconsistent with the fund's market timing policies,

(c) to assure that the intermediary is correctly assessing any redemption fees, and

(d) to assure consistent enforcement of the fund's market timing policies.

The Commission should require each mutual fund to adopt rigorous polices and procedures, and to subject itself to annual audits, to assure compliance with this restriction.

Detailed Comments

1. The Commission should impose uniform share aging and tracking requirements for all purposes under rule 22c-2. Specifically, the Commission should provide that, for both reporting and redemption fee purposes, mutual funds and financial intermediaries that are participant-directed individual account retirement plans must (i) use FIFO accounting and (ii) disregard all transactions by participant-directed individual account retirement plans other than participant-directed investment transfers. For example, in imposing a redemption fee, a fund should be required to disregard purchases and redemptions attributable to --

   (a) the plan's receipt of employee and employer contributions, rollovers, and loan payments,

   (b) distributions, withdrawals, rollovers, and loans from the plan,

   (c) plan mergers, spin-offs, and terminations and plan-to-plan transfers, and

   (d) automatic portfolio rebalancing.[6]

   Likewise, the administrators and recordkeepers of participant-directed individual account retirement plans should be required to disregard such transactions for reporting purposes under rule 22c-2(a)(2)(i).

As the Commission recognized in the proposing release, the vast majority of mutual fund investors do not pursue short-term trading strategies; a small percentage of shareholders account for most of the active trading in mutual fund shares.[7]

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[6] In general, when a fund includes an automatic portfolio rebalancing feature, the fund invests in two or more funds (*e.g.*, an equity fund, a bond fund, and a money market fund), and automatically rebalances its portfolio whenever the total fund diverges from its target allocation (*e.g.*, 70% equities, 25% bonds, and 5% money market) by more than a prescribed margin (*e.g.,* 5 percentage points). Some funds (sometimes referred to as "lifecycle funds") are designed to meet the needs of participants expecting to retire in a specified year and automatically rebalance as the designated retirement year draws closer (*e.g.*, by allocating an increasing percentage of the portfolio to bonds and money market funds and a declining percentage to equities). Although an individual participant can decide whether the participant wishes to allocate all or part of his or her account to such a fund, the participant has no control over the operation of the fund's automatic portfolio rebalancing feature. Automatic portfolio rebalancing may occur at either the participant level or the fund level. If it occurs at the participant level, the participant's interests in two or more funds are periodically rebalanced. If it occurs at the fund level, a participant might invest, for example, in a single "fund of funds" and that fund's interests in the funds in which it invests are periodically rebalanced.

Nevertheless, the reporting requirements and redemption fees imposed under rule 22c-2 might apply to many routine transactions that are not used to implement short-term trading strategies, such as (a) purchases and redemptions attributable to the plan's receipt of contributions, rollovers, and loan payments, (b) distributions, withdrawals, rollovers, and loans from the plan, (c) plan mergers, spin-offs, and terminations and plan-to-plan transfers, and (d) automatic portfolio rebalancing. Under the rule, a retirement plan is required to track the amounts and dates of all purchases and redemptions or exchanges for each participant. Moreover, each plan is required to comply with the method designated by each mutual fund for assuring that the plan's reports to the fund are accurate and that any appropriate redemption fees are imposed. If -- as is frequently the case -- a retirement plan offers funds sponsored by different mutual fund families, the plan could be required to use completely different methods for reporting to the funds and imposing redemption fees.

The costs of compliance could be enormous. Each plan will be required to track the date when each share was acquired, the number of shares acquired on each date, which participant or beneficiary acquired the shares, and the date when each share is deemed redeemed. Moreover, because the rule allows each fund (a) to set a holding period of longer than seven days, (b) to designate the purchases and redemptions taken into account, and (c) to designate the rate at which the fee will be imposed, funds are bound to apply the redemption fee differently. The computer programming, recordkeeping, and other administrative costs that will be borne by plans that must accommodate the demands of each mutual fund that they offer are likely to be staggering.

These costs will be borne by plan participants -- the vast majority of whom do not pursue short-term trading strategies. ERISA allows reasonable plan administration expenses to be paid by the plan.[8] If an individual account plan pays administration expenses, as is typically the case, the expenses borne by the plan reduce the value of each participant's and beneficiary's plan account. Some employers pay plan administration expenses out of their own assets; however, because employers have limited compensation and benefits budgets, any additional plan administration expenses borne by employers will inevitably reduce the employee compensation and benefits that those employers would otherwise provide.

Because enormous compliance costs will reduce the retirement income of millions of retirement plan participants, the Commission should do everything it can to reduce those costs and thereby avoid reducing the retirement income of millions of retirees. As we have noted, the vast majority of retirement plan participants do not engage in short-term trading; indeed, retirement plan participants are among the intended beneficiaries of the Commission's new rule. The Commission should not issue a rule that is likely to harm the millions of retirement plan participants whom the rule is designed to protect.

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[7] 69 Fed. Reg. 11,764 n.24 (March 11, 2004).

[8] ERISA §§ 403(c)(1), 404(a)(1)(A).

Rule 22c-2 should be modified to mandate the use of the FIFO accounting method (the method used by the overwhelming majority of funds that impose redemption fees) and to require fund redemption fees (and financial intermediaries' reports) to target the types of transactions that are used to implement short-term trading strategies: participant-directed investment transfers. If the Commission does this, the rule will be better focused on short-term trading activity, compliance with the rule will be simplified and enhanced, plan costs will be reduced, and plan participants' retirement savings will be protected, all in a manner that advances the rule's objective of protecting long-term investors from bearing the costs of other investors' short-term trading strategies.

Mandating FIFO accounting and targeting participant-directed investment transfers will have an important advantage over and above cost-savings: participants will understand the rationale for any fees that are imposed on them. If redemption fees apply only on a FIFO basis and only to participant-directed investment transfers, the fees will apply to very few participants, and it will be easy to explain to affected participants why they must pay the fees. On the other hand, if the rule allows redemption fees to apply to routine transactions (*e.g.,* portfolio rebalancing transactions, loans, and loan repayments), participants will be bewildered and discouraged from plan participation. The Commission should adopt a rule that advances, rather than undermines, the important public policy objective of encouraging retirement savings.

Assuming that the Commission modifies the rule to target only participant-directed investment transfers (so that certain purchases and redemptions, such as payroll deduction contributions, must be disregarded when imposing a redemption fee), any redemption fee should be applied on the basis of a *modified* FIFO rule. Under the *modified* FIFO rule, redemptions would be applied (1) first against disregarded shares (shares initially purchased with, for example, employee contributions, rollovers, and plan-to-plan transfers), (2) then against nondisregarded, mature shares (shares that have been held long enough to be exempt from the fund's redemption fee), and (3) lastly against nondisregarded, immature shares (shares that have not yet been held for the holding period prescribed by the fund). A redemption fee would apply only to shares in the last category.

2. There will be no need for a "de minimis" rule or for waivers if the Commission adopts the recommendation in paragraph 1, above.

An additional advantage of the recommendation in paragraph 1 is that it will eliminate the need for a "de minimis" rule or for waivers. In combination, FIFO accounting and a focus on participant-initiated investment transfers will cause retirement plans' transaction reports and funds' redemption fees to apply only in appropriate cases.

3. The Commission should not fix the rate at which a mutual fund must impose any redemption fee nor should the Commission specify the length of time that mutual fund shares must be held in order to avoid any redemption fee.

Although ERIC does not object to the 2% ceiling on a redemption fee, ERIC recommends that the Commission not fix the redemption fee rate. Some funds may conclude that, although it is necessary or appropriate to impose a redemption fee, the fund's needs will

be met by a lower rate. A fixed rate would deprive retirement plan participants and other investors of the benefit of the lower rate for such funds.

Likewise, because the length of the appropriate holding period will vary from fund to fund, the Commission should not specify a uniform holding period for all funds imposing a redemption fee. A "one-size-fits-all" approach will likely produce a uniform holding period that is longer than necessary for some funds (and therefore unnecessarily restrictive for the retirement plan participants who participate in that fund) and shorter than necessary for others (and therefore not sufficiently protective of the interests of the vast majority of investors, including retirement plan participants).

We understand that although some retirement plans' information technology systems will require additional programming in order to accommodate variations in redemption fee rates and holding periods, most retirement plans are now (or soon will be) able to accommodate variations in redemption fee rates and holding periods without great difficulty.

4. <u>The Commission should amend rule 22c-2(a)(2)(i) to provide that an agreement between the fund (or its principal underwriter) and a retirement plan administrator or recordkeeper need not require the administrator or recordkeeper</u> --

    (a) <u>to respond to more than one request by the fund per month</u>,

    (b) <u>to furnish information that it has previously furnished to the fund, or</u>

    (c) <u>to furnish information relating to transactions that occurred more than 12 months before the date of the request</u>.

Rule 22c-2(a)(2)(i) requires each mutual fund (or its principal underwriter) and each of its financial intermediaries to enter into an agreement that requires the intermediary to "provide, promptly upon request by the fund," the taxpayer identification numbers of all those who purchased, redeemed, transferred, or exchanged shares held through an account with the intermediary and the amounts involved in, and dates of, such transactions.

The rule does not make clear whether the agreement may impose conventional and commercially reasonable limits on the frequency with which the fund may make such requests, on the fund's ability to make repeated requests for information it has already received, or on the time period covered by any such request. If an agreement is not permitted to impose such limits, retirement plans will be required, as a practical matter, to develop the capacity -- and to incur the attendant costs -- to respond to frequent, redundant, and overbroad requests, even if the mutual funds in which they invest do not intend to make such requests. As we have explained, plan participants can be expected to bear any additional administrative costs that are imposed on the plan in the first instance.

We urge the Commission to make clear that the agreement may impose reasonable limits on the fund's ability to make frequent, redundant, or overbroad requests.

We are recommending only that the Commission provide that a fund *is permitted to* enter into an agreement that includes such limits. If the fund's management believes that one or more of the limits will prevent the fund's management from discharging its duties to the fund's shareholders, the fund's management can refuse to include the limit(s) in the fund's agreements with retirement plan administrators; retirement plan administrators can respond to any such refusal either (i) by agreeing to the fund's position or (ii) by refusing to enter into an agreement with the fund (and, presumably, by investing in another fund(s)).

5. The Commission should amend rule 22c-2(a)(2)(ii) to provide that an agreement between the fund (or its principal underwriter) and a retirement plan administrator or recordkeeper may, if the parties to the agreement so choose, impose reasonable restrictions on the instructions that the fund may issue, including --

    (a) a requirement that the fund's instructions be reasonable (for example, with respect to their effective date),

    (b) restrictions designed to assure that the plan and its fiduciaries and administrators comply with applicable law (such as the applicable provisions of ERISA (including the regulations under ERISA § 404(c)) and the Internal Revenue Code),

    (c) a requirement that the fund furnish to the plan administrator or recordkeeper a written explanation of the reason for its instruction,

    (d) a provision that gives the plan administrator or recordkeeper an opportunity to verify the fund's explanation of the reason for its instruction, and

    (e) a provision allowing any dispute between the fund and the plan administrator or recordkeeper regarding the fund's instructions to be submitted to an independent party for resolution pursuant to an alternative dispute resolution ("ADR") process.

Rule 22c-2(a)(2)(ii) states that the required agreement between a mutual fund (or its principal underwriter) and each of its financial intermediaries must provide that the intermediary will "execute any instructions" that the intermediary receives from the fund to restrict or prohibit future purchases or exchanges of fund shares by a party that the fund identifies as having engaged in transactions that violate fund policies.

Although the rule does not refer to the possibility that the agreement might impose conventional and commercially reasonable limits on such instructions, plan administrators and recordkeepers cannot reasonably be expected to agree in advance to execute *any* instructions that they receive from a mutual fund. For example, as a matter of fiduciary responsibility to plan participants, many plan fiduciaries will insist on receiving and double-checking documentation supporting the fund's instructions and will want to confirm that the instruction is lawful and does not jeopardize either the plan's status as a participant-directed plan under ERISA § 404(c) or the plan's tax qualification. Furthermore, in some cases, the plan administrator or recordkeeper will dispute the fund's instruction (for example, where the administrator or recordkeeper believes that the fund's instruction was issued in

error or where the fund failed to give advance notice of the policy that it alleges to have been violated).

The Commission should make clear that the agreement between the fund and the administrator or recordkeeper may include provisions that reasonably address these problems. We are recommending only that the Commission provide that a fund *is permitted to* enter into an agreement that includes such provisions. If the fund's management believes that such provisions will prevent the fund's management from discharging its duties to the fund's shareholders, the fund's management can refuse to include the provisions in the fund's agreements with retirement plans; retirement plans can respond to the fund's position either (i) by agreeing to the fund's position or (ii) by refusing to enter into an agreement with the fund (and, presumably, by investing in another fund(s)).

6. The Commission should amend rule 22c-2(a)(2) to provide that a retirement plan administrator or recordkeeper may agree to furnish information to a fund, or to comply with the fund's instructions, in accordance with the rule only if the fund agrees to reimburse the administrator or recordkeeper for any additional expenses that the administrator or recordkeeper incurs in complying with the fund's request for information or the fund's instructions.

If the costs of complying with funds' requests and instructions are not borne by the funds issuing the requests and instructions, funds will be shielded from a powerful incentive to issue only reasonable and necessary requests and instructions. Moreover, if the costs of compliance are not borne by the funds, plan administrators and recordkeepers will, in one way or another, pass these costs on to plan participants -- who are a small subset of the investors who will benefit from the fund's actions. Because the investment made by any one plan represents a tiny fraction of the total investment in a typical mutual fund, it is appropriate for the fund -- and its investors -- to bear the costs of complying with the fund's requests and instructions.

7. The Commission should expressly forbid a mutual fund from using, directly or indirectly, any information that a retirement plan administrator or recordkeeper furnishes to the fund in accordance with a rule 22c-2(a)(2) agreement for any purpose other than one of the purposes identified by the Commission:

    (a) to monitor trading,

    (b) to identify those who engage in frequent trading that is inconsistent with the fund's market timing policies,

    (c) to assure that the intermediary is correctly assessing any redemption fees, and

    (d) to assure consistent enforcement of the fund's market timing policies.

The Commission should require each mutual fund to adopt rigorous polices and procedures, and to subject itself to annual audits, to assure compliance with this restriction.

In the adopting release, the Commission stated that --

> "Our privacy rule prevents a fund that receives this information from using the information for its own marketing purposes, unless permitted under the intermediary's privacy policies. *See* 17 CFR 248.11(a) and 248.15(a)(7)(i)."[9]

The Commission should go much farther. Mutual funds should be barred from using the information furnished to them by retirement plans for any purpose other than a purpose identified by the Commission: to monitor trading, to identify those who engage in frequent trading that is inconsistent with the fund's market timing policies, to assure that the intermediary is correctly assessing any redemption fees, and to assure consistent enforcement of the fund's market timing policies.[10]

Employers and employees assign great value to employee privacy. The information furnished by a retirement plan to a mutual fund in accordance with a rule 22c-2 agreement should not be used by the mutual fund for any purpose other than a purpose that the rule was designed to serve. Broader use would infringe on employee privacy and would not serve any objective of either the Investment Company Act or ERISA. Employees should not be required to surrender their privacy in order to invest their retirement savings in a mutual fund.

The Commission should require mutual funds to be vigilant in protecting employee privacy. Each mutual fund should be required to adopt rigorous polices and procedures, and to subject itself to annual audits, to assure that employees' privacy interests are protected.

We very much appreciate the opportunity to submit these comments. We look forward to working with the Commission and its staff on this very important subject.

THE ERISA INDUSTRY COMMITTEE

[9] 70 Fed. Reg. 13,332 n.47.

[10] 70 Fed. Reg. 13,332.