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June 10, 2009

Ms. Elizabeth M. Murphy, Secretary  
Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549-1090

Re: FINRA's Proposed Rule 2231,  
Customer Account Statements; File  
No. SR-FINRA-2009-028

Dear Ms. Murphy:

The Investment Company Institute<sup>1</sup> appreciates the opportunity to comment on proposed FINRA Rule 2231 relating to customer account statements.<sup>2</sup> This rule, which is part of FINRA's ongoing efforts to consolidate NASD and NYSE rules, would require that customers be provided more frequent account statements – *i.e.*, monthly instead of quarterly. The Institute supports FINRA's efforts, as part of this consolidation process, to review and update its rules to ensure that they reflect current industry practices, advance investors' interests, and strike an appropriate balance between a rule's costs and its benefit to investors.

The Institute has long supported ensuring that the information provided to mutual fund shareholders regarding their accounts or investments best serves their interest. Consistent with our interest in best serving the needs of mutual fund investors, we strongly recommend that FINRA revise proposed Rule 2231 to except mutual fund accounts from the newly proposed monthly statement requirement. In addition, we strongly recommend that FINRA reconsider including provisions in Supplementary Material .01 to Rule 2231 that are inconsistent with Regulation S-P. The reasons for our recommendations are detailed below.

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<sup>1</sup> The Investment Company Institute is the national association of U.S. investment companies, including mutual funds, closed-end funds, exchange-traded funds (ETFs), and unit investment trusts (UITs). ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. Members of ICI manage total assets of \$10.18 trillion and serve over 93 million shareholders.

<sup>2</sup> See *Proposed Rule Change to Adopt FINRA Rule 2231 (Customer Account Statements) in the Consolidated FINRA Rulebook*, SEC File SR-FINRA-2009-028 (May 2009) ("FINRA's submission").

## OVERVIEW

As proposed, Rule 2231 would require all FINRA members that conduct a general securities business and compute their net capital pursuant to Rule 15c3-1(a) under the Securities Exchange Act of 1934 to begin sending monthly – rather than quarterly – statements to customers. According to FINRA’s submission, its proposal to replace the current quarterly statement requirement with a monthly requirement “better reflects current industry practice as a significant number of members already send customers monthly account statements through their clearing firm.” In addition to information about holdings and transactions, Supplementary Material .03 accompanying the proposal would require these monthly statements to disclose specified information about the member’s introducing and clearing firms and the fact “that the clearing firm is a member of SIPC.”<sup>3</sup>

The Institute is writing to respectfully request that the final version of Rule 2231 except mutual fund account statements from the monthly account statement requirement. Indeed, contrary to what may be “current industry practice” for general securities members, *quarterly account statements remain the standard industry practice in the mutual fund industry*. In large part, this is because of the current – and longstanding – consistency between existing NASD Rule 2340 and Rule 10b-10 under the Securities Exchange Act of 1934, as well as with Section 1025 of the Pension Protection Act of 2006<sup>4</sup> – each of which impose a quarterly reporting requirement.

## RULE 10B-10

Rule 10b-10 governs confirmation of transactions. While it generally requires all brokers and dealers to disclose specified information in writing to customers before the completion of a transaction, it includes special alternative periodic reporting provisions for “investment company plans.” (See Rule 10b-10(b)(2) and (d)(6)<sup>5</sup>.) Rather than receiving a confirmation in connection with each transaction effected pursuant to an investment company plan, investors holding these accounts receive *quarterly*

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<sup>3</sup> See Supplementary Material .03, Information to be Disclosed on Statement. Mutual funds do not utilize the services of “clearing firms,” nor are they required to be members of SIPC. See 15 U.S.C. §78ccc(a)(2)(A)(i), which expressly excepts persons whose business as a broker or dealer consists exclusively of the distribution of shares of registered open end investment companies or unit investment trusts from SIPC membership. While such dealers compute their net capital pursuant to Rule 15c3-1(a)(2)(v) under the Securities Exchange Act of 1934, they are not typically registered with FINRA to conduct a general securities business.

<sup>4</sup> Though the quarterly statement requirement applicable to pension accounts was only added to federal law in 2006, quarterly account statements have long been the norm for these accounts.

<sup>5</sup> Generally speaking, the term “investment company plan” means plans under which registered mutual fund or unit investment trust shares are sold pursuant to retirement accounts as well as contractual or systematic agreements under which the customer purchases shares on a regular pre-arranged basis, including through dividend reinvestments.

statements detailing all transactions effected in their account during the quarter.<sup>6</sup> The consistency in the quarterly frequency of Rule 10b-10 and NASD Rule 2340 has resulted in FINRA's members satisfying their regulatory requirements under both of these provisions by providing mutual fund shareholders quarterly statements disclosing their transactions for the quarter as well as their holdings. Accordingly, while FINRA's general securities members that cannot take advantage of the alternative periodic reporting may have moved towards a monthly statement cycle, the same is not true of the mutual fund industry. To impose a monthly requirement on mutual fund accounts held by broker-dealers would disrupt current systems and practices at great expense to investors, who ultimately must bear the costs associated with this new requirement.

### **THE PENSION PROTECTION ACT OF 2006**

A monthly statement requirement would also go beyond the requirements of the Pension Protection Act. Section 1025 of the Pension Protection Act of 2006 requires that investors in participant-directed 401(k) plans subject to ERISA receive quarterly statements.<sup>7</sup> The Institute estimates that there are currently approximately 62 million 401(k) participant accounts. To require each of these account holders to be provided a monthly statement – instead of the quarterly statements called for under the Pension Protection Act – would require significant changes to industry systems and processes at great costs to investors without providing them any meaningful benefit in return.

### **COSTS V. BENEFITS TO SHAREHOLDERS**

If the benefits associated with providing mutual fund shareholders, including retirement account holders, monthly account statements outweighed the costs, perhaps the shift from quarterly statements to monthly statements would be justified. This does not appear to be the case, however. Other than reinvesting dividends and capital gains distributions, the typical retail mutual fund account has very few transactions. For example, a 2006 study found that 62 percent of such accounts made no additional purchases in the first year after an account was opened, and 73 percent of accounts made no additional purchases in the second year after an account was open.<sup>8</sup> As such, it would appear that the

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<sup>6</sup> Mutual fund shareholders who purchase or redeem shares outside of an investment company plan receive a confirmation at the time of their transaction and quarterly statements thereafter. In other words, the systems our members use to produce and distribute account statements to all mutual fund accountholders are designed for quarterly statements. The confirmations and quarterly statements the accountholders currently receive regarding their mutual fund transactions provide them information about their transactions in a manner that would allow them “to review their statements in a timely manner for errors, possible identity theft or other potential problems,” as intended by the proposed monthly account statement requirement. *See* FINRA submission at p. 17.

<sup>7</sup> *See* 239 U.S.C. 1025(a).

<sup>8</sup> *See* Johnson, Woodrow T. and Brian Reid, “The Portfolio Choice of Individual Shareholders in Large Mutual Fund Families” (March 15, 2006).

current practice in the industry, which is to send quarterly statements, satisfies the needs of mutual fund shareholders. Moreover, those investors interested in more current account information likely have immediate access to it via toll-free phone numbers or mutual fund websites. Aside from burdening all mutual fund shareholders with additional, unnecessary statements each month, tripling the number of statements they receive will significantly increase the costs associated with these accounts, without providing any concomitant benefit.

These costs should not be underestimated. Aside from the extensive systems redesign this change would necessitate, they include the costs associated with producing, printing, stuffing, and mailing the additional statements. **Considering there are approximately 93 million individual mutual fund shareholders, increasing by three-fold the number of statements each one receives annually could result in the production of as many as 748 million unnecessary additional statements each year. Postage costs alone for these additional statements will be in the hundreds of millions of dollars.**<sup>9</sup> Moreover, aside from the costs incurred to implement this proposal, there likely will be a significant cost to the environment from tripling the number of account statements that must be produced and sent to investors.

It bears remembering that, when Rule 10b-10 was first proposed in 1976, it included the special provisions discussed above that permit mutual fund transactions to be confirmed quarterly through alternative periodic reporting.<sup>10</sup> In connection with this quarterly exception for investment company plan transactions, the Commission noted that “[s]ince the costs of regulation designed to promote investor protection are in the final analysis paid for in large part by the investor, the Commission is

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<sup>9</sup> One medium-sized member of the Institute noted that they currently send out 3 million statements a year. Under FINRA’s proposal, they would expect to send out 9 million statements a year, imposing approximately \$20 million in additional costs on investors. In light of the short comment period associated with FINRA’s proposal, the Institute is unable to provide more complete cost information. Our members are, however, quite concerned about the fiscal impact this proposal will have on their shareholders.

<sup>10</sup> The exception for shares of mutual funds was first adopted in 1974 as part of SEC Rule 15c1-4, which was the predecessor to Rule 10b-10. In 1976, the SEC repealed Rule 15c1-4 and adopted Rule 10b-10 in its place to govern confirmation requirements. See SEC Release No. 34-12806 (Sept. 16, 1976), which adopted Rule 10b-10, and SEC Release No. 34-13661 (June 23, 1977), which modified Rule 10b-10’s requirements to facilitate the use of quarterly statements in connection with mutual fund transactions. Prior to the 1976 revisions, to utilize the rule’s quarterly statement provisions, a prospectus would have to be delivered with each quarterly statement. Of concern to the SEC, however, was that “the quarterly statement procedure was not being used.” According to the Release, “it was suggested that certain costs associated with the administration of confirmation procedures generally outweighed the benefit of establishing new procedures for using quarterly statements.” To address these concerns and facilitate the use of quarterly confirmations, the Commission relaxed some of the conditions in Rule 10b-10 that had discouraged their use. See SEC Release 34-13661 at p.18.

endeavoring to adjust regulatory requirements to eliminate those for which compliance costs appear to be disproportionate to the practical benefits of investor protection thereby obtained.”<sup>11</sup>

We respectfully submit that the costs associated with FINRA’s current proposal will be grossly disproportionate to any practical or meaningful benefit to mutual fund investors, including those holding mutual funds through a retirement account. Indeed, courts have long recognized that mutual funds are long term investments and frequent transactions should not be encouraged.<sup>12</sup> As such, there does not appear to be the same need for mutual fund investors to receive monthly statements of their accounts as there may be for those investors holding brokerage accounts who may be regularly trading in and out of such accounts. Nor are such statements necessary to detect “error, identity theft,<sup>13</sup> or other potential problems.” Indeed, we are not aware of any complaints raised by mutual fund investors in these areas that would warrant all mutual fund investors receiving monthly account statements. Also, as pointed out above, for the small percentage of investors who make discrete, individual trades from time to time in their mutual fund accounts, Rule 10b-10 requires that they promptly receive a confirmation of the transaction, which would provide them access to important information concerning such transactions.

#### **SERVING THE INTERESTS OF SHAREHOLDERS**

The Institute has long advocated effective and timely disclosure for mutual fund shareholders. Consistent with this, we believe the account statements provided to mutual fund shareholders should provide them relevant information in a timely fashion. The existing practice of providing shareholders quarterly statements meets this standard. If monthly statements were necessary to protect the interests of mutual fund investors, we likely would be supportive of tripling the frequency of sending such statements. However, this is not the case. As noted above, the vast majority of mutual fund shareholders do not regularly purchase and redeem shares in their accounts. As such, there is no purpose to be served by informing them monthly that there has been no activity in their account. For the small percentage of shareholders who have account activity, either it is consistent activity pursuant to an investment company plan or it is sporadic activity. The former would receive quarterly confirmations pursuant to Rule 10b-10 and a quarterly account statement should satisfy their needs. The latter would receive a confirmation in connection with each discrete transaction and a quarterly

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<sup>11</sup> See SEC Release 34-12806.

<sup>12</sup> See *Krull v. SEC.*, 248 F.3d 907, 912 (9<sup>th</sup> Cir. 2001).

<sup>13</sup> The requirements of the USA PATRIOT Act, including the anti-money laundering and Customer Identification Program (CIP) requirements, as well as requirements under the Red Flag Rules of the Federal Trade Commission are better geared to protect investors from identity theft than a monthly account statement requirement.

statement thereafter, so receiving a statement each and every month is not necessary to protect their interests. Moreover, as previously noted, those investors who are interested in more frequent account information likely have immediate access to it via toll-free phone numbers or fund websites.

For all of the above discussed reasons, the Institute strongly recommends that FINRA revise proposed Rule 2231 to better serve the interests of shareholders by expressly excepting mutual fund account statements, including those provided to 401(k) accountholders, from the monthly statement requirement.<sup>14</sup>

#### **SUPPLEMENTARY MATERIAL .01, TRANSMISSION OF CUSTOMER STATEMENTS**

In addition to our above discussed concerns with the application of Rule 2231 to mutual fund accounts, we are concerned with how Supplementary Material .01 might impede the legitimate sharing of information that occurs in connection with processing, servicing, and maintaining such accounts. As proposed, Supplementary Material .01 would prohibit a FINRA member from providing a copy of an account statement, confirmation, or other communication relating to a customer's account to any person other than the customer without the customer's express written instruction to do so. According to the explanation of this provision, it is based on NYSE Rule 409(b), which expressly requires firms to obtain written instructions from a customer prior to sharing the customer's information.

This provision in Rule 409(b) appears to predate enactment of provisions in the Gramm-Leach-Bliley Act and Regulation S-P thereunder that govern the sharing of information in the securities industry. As applied to transactions and accounts involving mutual fund shares, this Supplementary Material would impede the use of current systems necessary to effect, service, and maintain customer transactions. (Even sharing the information necessary to produce the required statements could run afoul of this prohibition.) For example, it is not uncommon for a financial adviser that effects a mutual fund transaction on behalf of a customer to receive a copy of information provided by the mutual fund company to the customer for purposes of servicing the customer's account. As proposed, Supplementary Material .01 would preclude this necessary sharing of information in the absence of a customer's express written consent. Such a requirement would impact the tens of millions of mutual fund accounts in existence today by disrupting ongoing sharing arrangements between mutual funds and their distributor networks until such time as FINRA members could obtain the written approval of their millions of customers. (Particularly for existing accounts, this is likely to be a lengthy and expensive process.) Moreover, the inability of a member to timely obtain such consent could impede

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<sup>14</sup> This could be accomplished by amending 2231(a) in relevant part to read: "... with a frequency of not less than once every calendar month, to each customer, other than a customer who purchases or redeems shares in a registered investment company, whose account had account activity during the period since the last such statement was sent to the customer, and with a frequency of not less than once every calendar quarter to each customer who purchases or redeems shares in a registered investment company and each customer whose account had a security position or money balance during the period since the last such statement was sent to the customer."

the financial adviser's ability to effectively monitor and service the account in the interim, to the detriment of the shareholder.

In light of the existence of the GLB Act and Regulation S-P, this requirement is wholly unnecessary. Indeed, for almost ten years, Federal law has precluded the sharing of information unless expressly permitted pursuant to the Act or exceptions in the Regulation. Currently, such sharing typically occurs pursuant to the Regulation's exception that permits sharing information as necessary to process or service transactions (Section 248.14) or for other specified purposes (*e.g.*, to detect or prevent fraud). As Regulation S-P was expressly adopted to protect the security and confidentiality of *all* non-public personal information about consumers, it seems unnecessary to include a specific provision in FINRA's rules addressing this issue only with respect to account statement information. Moreover, including this prohibition in FINRA's rules would result in an inconsistency between FINRA's rule and the Regulation's requirements, which would impose additional and costly burdens on the lawful sharing of information that is necessary to process customer transactions and service and maintain customer accounts. Accordingly, we strongly recommend that FINRA either delete Supplementary Material .01 from its proposal or revise it to permit the sharing of customer account statements, confirmations, or other communications relating to a customer's account to the extent permitted under Regulation S-P.<sup>15</sup>

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The Institute appreciates the opportunity to provide these comments on its proposal. If you have any questions concerning these comments or would like additional information, please contact the undersigned by phone (202-326-5825) or email ([tamara@ici.org](mailto:tamara@ici.org)).

Sincerely,

/s/ Tamara K. Salmon

Tamara K. Salmon  
Senior Associate Counsel

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<sup>15</sup> We also recommend that FINRA limit proposed Supplementary Material .03, Information to be Disclosed on Statement, to information that is applicable to the customer's account. For example, as discussed above, information regarding "the introducing firm and clearing firm" and SIPC membership would not be applicable to mutual fund accounts, and so should not be required to be disclosed on mutual fund statements.