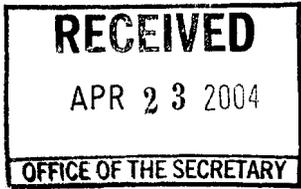


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MEMORANDUM

TO: Public Comment File No. S7-27-03
FROM: Adam B. Glazer
Office of Regulatory Policy
Division of Investment Management ("IM")
DATE: April 23, 2004



On April 16, 2004, representatives of Fidelity Investments ("Fidelity"), the American Society of Pension Administrators ("ASPA"), The Principal Financial Group, and The Depository Trust & Clearing Corporation ("DTCC") met with staff members of the U.S. Securities and Exchange Commission to discuss issues relating to the Commission's proposed rule amendments concerning the pricing of investment company shares in Investment Company Act Release No. 26288 (Dec. 11, 2003) ("Late Trading Proposal"). The following Commission staff members attended the meeting: Robert Plaze, Associate Director, IM; Hunter Jones, Assistant Director, IM; Penelope Saltzman, Branch Chief, IM; and Adam Glazer, Attorney, IM.

The representatives discussed three issues relating to the Late Trading Proposal and the central clearinghouse concept described in Fidelity's comment letter. Some of Fidelity's representatives had first discussed the central clearinghouse with staff members at a meeting on February 26, 2004, and representatives provided more details on the central clearinghouse at a March 16, 2004 meeting with staff. This alternative would limit same-day pricing to orders received by a clearinghouse (*i.e.*, NSCC) by 4 p.m.

The Fidelity representatives discussed two recommendations described in Fidelity's comment letter. First, they suggested the Commission provide an exception for funds of funds that invest only in funds within the same fund complex. Second, they recommended expanding the orders eligible for same-day pricing under the Late Trading Proposal to include orders received by 4 p.m. by transfer agents that are under common ownership with the designated transfer agent.

Finally, the Fidelity representatives recommended specific requirements to allow for the exclusion of a small percentage of retirement plan transactions that would not qualify for same-day pricing under the Late Trading Proposal, and that also would have difficulty qualifying for same-day pricing under the clearinghouse concept. The recommended requirements are described in Fidelity's attached outline.

Attachment

April 15, 2004

For retirement plans, the central clearinghouse represents a challenge for redemption transactions that require determination of account balance as a basis prior to transacting. These redemption transactions represent the minority of the total volume of all retirement plan transactions. Volumes have been estimated at less than 1% of total transactions and less than 9% of the total dollar value of all transactions processed in defined contribution plans.

This letter is sent to provide guidelines for an exemption in the SEC proposal for these redemption transactions. The material contained in this letter should be utilized to develop language and demonstrate a case for this exemption.

Background

The exemption is requested for the following reasons:

Redemption transactions are governed by IRS, DOL and ERISA guidelines

Regulations apply controls on the number of distributions an employee can take. The regulations determine the taxability of the distribution and whether or not tax penalties apply. These rules also cap the amount available for certain distribution types.

Redemption transactions are governed by plan rules

Plan rules determine the number of trades permitted. Plans also determine eligibility requirements and will detail the liquidation method for distribution transactions.

Availability for redemption transactions cannot be determined before the account is valued

The liquidation method for redemption transactions cannot be determined until the account is valued. Since the liquidation method determines taxability and penalties, it is critical that this information is correct. Also, the cap on transactions cannot be determined until the account is valued, nor can eligibility.

Redemption transactions do not lend themselves to opportunities for abuse

These transactions are generally one-time events with complex rules and liquidation methods. The number of variables involved (funds, money sources, liquidation methods plan rules and regulations) creates a tight control system around these transactions.

Transaction Types

The following represents a high level list of transactions that would fall into the exemption category. Each plan contains some variety of these transactions and can name them in a similar or different fashion:

- In-service withdrawal – under certain plans this type of withdrawal is available to active employees. Any pretax money distributed (or tax deferred earnings) are subject to an early withdrawal penalty.
- Hardship withdrawals – most plans allow employees to access their money for financial hardship. The employee must provide documentation backing up the hardship withdrawal. Employees are typically restricted from making further contributions to the plan for a period of time once they take this withdrawal.
- Retiree distributions – at age 59.5 retirement plans allow for distribution of assets. The liquidation method for these withdrawals is determined based upon plan rules. There could be requirements placed on these distributions.
- Minimum required distribution – these distributions are required once the employee reaches age 70.5. The amount of the participant’s account is used as a basis, along with the employee’s age to determine the amount of the distribution.
- Full distribution – Once separated from service, the employee has the right to request a full distribution of their account. The payout of an employees account in full requires that dividends have been applied. Dividends applied to account balances will impact the final value of the account.
- Loan withdrawals – Most plans allow participants to take a loan for general purposes or for the purpose of providing funds for a purchase of a primary residence. The total amount available for a loan is calculated based upon the account balance. Also, the liquidation method is determined based upon the account balance.
- Return of excess distribution – Required as a result of a plan’s failed nondiscrimination test or it could represent a return of contributions in excess of certain tax limitations.

Language for complex transaction exemption:

The following is provided as recommended text that would be included as an additional exception under Subsection (b) of the proposed rule:

(b)(6) Certain plan transactions.

(i) Subject to the conditions in (ii) below, a fund may deem receipt of a redemption order, other than an exchange order, to have occurred immediately before the applicable pricing time if the fund, its designated transfer agent, or a registered clearing agency receives the redemption order from a record keeper of an employee pension benefit plan as defined in Section 3(2)(A) of the Employee Retirement Income Security Act of 1974, or of a tax-sheltered annuity or custodial account program as defined in Section 403(b) of the Internal Revenue Code.

(ii) in order to rely on this exception:

- (a) The fund must have entered into a written agreement with the record keeper authorizing the record keeper to accept and transmit

- such redemption orders to the fund and requiring the record keeper to date and time stamp all such orders;
- (b) The record keeper must receive the redemption request on the pricing date prior to the applicable pricing time; and
 - (c) The record keeper must transmit a file containing the specifics of each transaction taken and the timing of the transaction to the fund, transfer agent or clearing agency on the date following pricing date.

Conclusion

It is not practical to impose a requirement on retirement plan redemption transactions that requires them to be delivered to the fund by 4:00. The basis for these transactions requires an end of day account valuation to calculate the transaction. Therefore, requiring the process to be completed prior to NAV determination would be impossible. Plans attract greater participant interest and retirement investment as a result of offering redemption transactions. A 4:00 hard close requirement imposed on these transactions could create access and liquidity concerns at the participant level.

A total exemption and status quo process on these transactions is not practical either. It is critical that an audit trail is created for these transaction types. As a result, these transactions, once taken, will flow through the system as they do today. At the end of the process, these transactions would be logged at the fund or clearinghouse. The fund would be provided full transparency on these transactions.