SECURITIES AND EXCHANGE COMMISSION

Release Nos. 33-10505; 34-83379; IC-33114; File No. S7-13-18

REQUEST FOR COMMENTS ON THE PROCESSING FEES CHARGED BY INTERMEDIARIES FOR DISTRIBUTING MATERIALS OTHER THAN PROXY MATERIALS TO FUND INVESTORS

AGENCY: Securities and Exchange Commission

ACTION: Request for comment.

SUMMARY: The Securities and Exchange Commission is seeking public comment on the framework under which intermediaries may charge fees for distributing certain non-proxy disclosure materials to fund investors, such as shareholder reports and prospectuses ("Fund Materials"), particularly where those fees may be borne by the fund and, in turn, its investors.

DATES: Comments should be received by October 31, 2018.

ADDRESSES: Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's internet comment form (*http://www.sec.gov/rules/other.shtml*); or
- Send an email to *rule-comments@sec.gov*. Please include File No. S7-13-18 on the subject line.

Paper comments:

- Send paper comments to Secretary, Securities and Exchange Commission, 100 F Street NE, Washington, DC 20549-1090.

All submissions should refer to File Number S7-13-18. This file number should be included on the subject line if email is used. To help the Commission process and review your comments more efficiently, please use only one method of submission. The Commission will post all comments on the Commission's website (*http://www.sec.gov*). Comments are also available for

website viewing and printing in the Commission's Public Reference Room, 100 F Street NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make publicly available.

FOR FURTHER INFORMATION CONTACT: J. Matthew DeLesDernier and John Lee, Senior Counsels, or Michael C. Pawluk, Senior Special Counsel, at (202) 551-6792, Investment Company Regulation Office, Division of Investment Management, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-8549.

SUPPLEMENTARY INFORMATION: The Securities and Exchange Commission ("Commission") is seeking public comment on the framework for fees charged by intermediaries for the distribution of Fund Materials to investors that are beneficial owners of registered investment company ("fund") shares held in "street name" through an intermediary.

I. INTRODUCTION

In a contemporaneous release, the Commission adopted rule 30e-3 under the Investment Company Act of 1940 ("Investment Company Act").[1] The rule provides certain funds with the ability to satisfy their obligations under the Investment Company Act to transmit shareholder reports by making the report and other materials accessible at a website address specified in a notice to investors.

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[1] 15 U.S.C. 80a-1 *et seq.*; Optional Internet Availability of Investment Company Shareholder Reports, Investment Company Act Release No. 33115 (June 5, 2018).

In connection with the proposal of rule 30e-3,[2] some commenters expressed concerns about the rules of the New York Stock Exchange ("NYSE") and other self-regulatory organizations ("SROs") such as the Financial Industry Regulatory Authority ("FINRA") under which intermediaries are permitted to seek reimbursement for forwarding shareholder reports and other fund materials to investors that are beneficial owners of shares held in "street name" through the intermediary.[3] One commenter particularly noted that the NYSE rules could result in increased processing fees that could negate potential costs savings related to the implementation of rule 30e-3.[4] In light of these concerns, in 2016 the NYSE submitted certain amendments to its rules concerning the application of these processing fees.[5] As part of that submission, the NYSE stated that the amendments were intended solely to facilitate the new

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2 Investment Company Reporting Modernization, Investment Company Act Release No. 31610 (May 20, 2015) [80 FR 33590 (June 12, 2015)].

3 FINRA has noted that its rules "correspond, in virtually identical language" to NYSE rules already adopted. FINRA Regulatory Notice 14–03 (Jan. 2014), *available at* http://finra.complinet.com/net_file_store/new_rulebooks/f/i/FINRANotice_14_03.pdf. As discussed below, these rules establish the maximum amount that a member of the respective organization may receive for distributing fund materials to beneficial owners as "reasonable expenses" eligible for reimbursement under rules 14b-1 and 14b-2 under the Exchange Act of 1934 ("Exchange Act") [15 U.S.C. 78a *et seq.*]. *See infra* Part II.B. Rules of other SROs also correspond to NYSE rules 451 and 465 and FINRA rule 2251 governing the maximum reimbursement that intermediaries are permitted to seek for forwarding Fund Materials, and throughout this Release unless the context requires otherwise, when referring to NYSE and/or FINRA rules, we are also referring to these related SRO rules. *See, e.g.*, NASDAQ rule 2251; NYSE MKT rule 576. Historically when NYSE initiates a rule change with respect to these fees, other SROs, including FINRA, follow with corresponding changes. Additionally, non-broker intermediaries, such as banks, generally rely on the NYSE rule 451 fee schedule. *See* Internet Availability of Proxy Materials, Securities Exchange Act Release No. 55146 (Jan. 22, 2007) [72 FR 4147, 4157 n.118 (Jan. 29, 2007)].

4 *See* Comment Letter of the Investment Company Institute (Mar. 14, 2016) on File No. S7-08-15, *available at* http://www.sec.gov/comments/s7-08-15/s70815.shtml ("2016 ICI Comment Letter"). Stakeholders have also discussed many of the concerns raised in connection with proposed rule 30e-3 in connection with other Commission releases. *See infra* Parts II–III.

5 *See* Exchange Act Release No. 78589 (Aug. 16, 2016) [81 FR 56717 (Aug. 22, 2016)] (Notice) ("2016 Amendments Notice"). We discuss below the changes made to the NYSE rule. *See infra* note 30 and accompanying text.

delivery method for fund shareholder reports permitted by rule 30e-3 as proposed by the Commission.[6] The NYSE did not, at that time, propose to make additional changes to its rules to address the other concerns expressed by the commenter and further stated that those concerns should be given separate consideration.[7]

In the past when we have approved changes to the NYSE's rules governing processing fees, we have emphasized that we expected the NYSE to continue to periodically review these fees to ensure they are related to reasonable expenses.[8] In particular, we observed that such monitoring is essential because technological advances should help to reduce processing costs in the future.[9]

With the adoption of rule 30e-3, we believe it is appropriate to consider more broadly the overall framework for the fees that broker-dealers and other intermediaries charge funds, as reimbursement for distributing Fund Materials to investors. A number of industry participants have expressed views regarding the appropriateness of the current framework as it relates to Fund Materials—which was designed primarily for delivery of operating company proxy materials. Specifically, commenters have raised issues including the clarity of SRO rules as they

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[6] 2016 Amendments Notice, *supra* note 5, at 56720.

[7] *Id.*; *see also infra* note 10 and accompanying text.

[8] *See* Order Approving Proposed Rule Change and Amendment No. 1 Thereto by the New York Stock Exchange, Inc. Amending Its Rules Regarding the Transmission of Proxy and Other Shareholder Communication Material and the Proxy Reimbursement Guidelines, Exchange Act Release No. 45644 (Mar. 25, 2002) [67 FR 15440, 15444 (Apr. 1, 2002)] ("2002 Amendments Approval"); Order Granting Approval to Proposed Rule Change Amending NYSE Rules 451 and 465, and the Related Provisions of Section 402.10 of the NYSE Listed Company Manual, Which Provide a Schedule for the Reimbursement of Expenses by Issuers to NYSE Member Organizations for the Processing of Proxy Materials and Other Issuer Communications Provided to Investors Holding Securities in Street Name, and to Establish a Five-Year Fee for the Development of an Enhanced Brokers Internet Platform, Exchange Act Release No. 70720 (Oct. 18, 2013) [78 FR 63530, 63531 (Oct. 24, 2013)] ("2013 Amendments Approval").

[9] 2002 Amendments Approval, *supra* note 8, at 63531.

apply to Fund Materials; the value of the services provided in exchange for the processing fees assessed; the degree to which SROs have tailored fees to reflect delivery of Fund Materials—as distinct from operating company proxy or other materials; the degree to which competition or its absence may affect the amount of the fees assessed; and the appropriate SRO to maintain oversight of such fees.[10]

The SRO rules governing processing fees and related out-of-pocket expenses are meant to reimburse intermediaries for the "reasonable expenses" they incur in forwarding materials to beneficial shareholders. These reimbursable amounts include the amounts intermediaries pay under contract to third-party service providers who deliver shareholder materials on their behalf. We understand that funds generally pay these reimbursements from their own assets as expenses of the fund.[11] We are seeking public comment and additional data on the framework for the fees

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[10] *See, e.g.*, 2016 ICI Comment Letter, *supra* note 4; Comment Letter of Ariel Investment Trust (Sept. 8, 2016) on File No. SR-NYSE-2016-55, *available at* https://www.sec.gov/comments/sr-nyse-2016-55/nyse201655.shtml ("2016 Ariel Letter"); Comment Letter of AST Fund Solutions (May 16, 2013) on File No. SR-NYSE-2013-07, *available at* https://www.sec.gov/comments/sr-nyse-2013-07/nyse201307.shtml ("2013 AST Letter"); Comment Letter of Columbia Mutual Funds (Sept. 15, 2016) on File No. SR-NYSE-2016-55, *available at* https://www.sec.gov/comments/sr-nyse-2016-55/nyse201655.shtml ("2016 Columbia Letter"); Comment Letter of Dimensional Fund Advisors LP (Sept. 12, 2016) on File No. SR-NYSE-2016-55, *available at* https://www.sec.gov/comments/sr-nyse-2016-55/nyse201655.shtml ("2016 Dimensional Letter"); Comment Letter of Invesco Advisers, Inc. (Sept. 12, 2016) on File No. SR-NYSE-2016-55, *available at* https://www.sec.gov/comments/sr-nyse-2016-55/nyse201655.shtml ("2016 Invesco Letter"); Comment Letter of the Investment Company Institute (Sept. 12, 2016) on File No. SR-NYSE-2016-55, *available at* https://www.sec.gov/comments/sr-nyse-2016-55/nyse201655.shtml ("2016 ICI Letter II"); Comment Letter of the Investment Company Institute (Mar. 15, 2013) on File No. SR-NYSE-2013-07, *available at* https://www.sec.gov/comments/sr-nyse-2013-07/nyse201307.shtml ("2013 ICI Letter"); Comment Letter of MFS Investment Management (Sept. 12, 2016) on File No. SR-NYSE-2016-55, *available at* https://www.sec.gov/comments/sr-nyse-2016-55/nyse201655.shtml ("2016 MFS Letter"); Comment Letter of T. Rowe Price Associates (Sept. 12, 2016) on File No. SR-NYSE-2016-55, *available at* https://www.sec.gov/comments/sr-nyse-2016-55/nyse201655.shtml ("2016 T. Rowe Letter").

[11] *See* Comment Letter of the Independent Directors of the BlackRock Equity-Liquidity Funds (Sept. 27, 2016) on File No. SR-NYSE-2016-55, *available at* https://www.sec.gov/comments/sr-nyse-2016-55/nyse201655.shtml; 2016 ICI Letter II, *supra* note 10.

charged by broker-dealers and other intermediaries for the distribution of Fund Materials to investors to better understand the potential effects on funds and their investors.

II. OVERVIEW OF CURRENT FRAMEWORK FOR FORWARDING FUND MATERIALS

A. "Street Name" Account Arrangements

Today, most fund investors are beneficial owners of shares held in "street name" through a "securities intermediary," such as a broker-dealer or bank.[12] When investors hold shares directly with their fund as registered or "record" owners, the fund's transfer agent maintains the names and addresses of the investors in its records. On the other hand, when an investor's shares are held in street name through an intermediary, the intermediary maintains the records of beneficial ownership. Such an investor has the ability to instruct its intermediary to withhold his or her personally identifying information from the issuers of securities that he or she owns.

A fund required or wishing to communicate with those investors has to rely on the intermediary to either forward the materials to the investor or, at the fund's request, the intermediary provides a list of non-objecting investors to the fund so that it may do so. To promote direct communication between funds (and other issuers of securities) and their investors, we have adopted rules to require intermediaries to provide funds, at their request, with

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[12] For purposes of this release, we use the terms "intermediary" to refer to a "securities intermediary" and "investors" to refer to beneficial owners of fund shares held through intermediaries. *See* 17 CFR 240.17Ad-20; Concept Release on the U.S. Proxy System, Exchange Act Release No. 62495 (July 14, 2010) [75 FR 42982, 42985 n.30 (July 22, 2010)] ("Proxy Mechanics Concept Release"); *compare* rule 22c-2 under the Investment Company Act (recognizing a number of different types of "financial intermediaries," such as broker-dealers, banks, insurance companies, and retirement plan administrators).

Approximately 75 percent of accounts in mutual funds are estimated to be held in street name. *See* Comment Letter of the Securities Industry and Financial Markets Association (Aug. 11, 2015) on Investment Company Reporting Modernization, File No. S7-08-15, *available at* http://www.sec.gov/comments/s7-08-15/s70815.shtml. In 2010, we estimated that 70 to 80 percent of all public issuers' shares are held in street name. Proxy Mechanics Concept Release, at 42999.

lists of the names and addresses of investors who did not object to having such information provided to issuers, often referred to as "non-objecting beneficial owners" (or "NOBOs").[13] However, many investors whose shares are held in street name accounts are "objecting beneficial owners" (or "OBOs") and may be contacted only through the intermediary (or its agent) that has the relationship with and is servicing the investor.[14]

Intermediaries generally outsource their fund delivery obligations to a third-party service provider that provides fulfillment services.[15] The fulfillment service provider enters into a contract with the intermediary and acts as a billing and collection agent for that intermediary.

B. Current Commission Rules Concerning Delivery or Transmission of Issuer Materials to Intermediated Accounts

Under Exchange Act rules 14b-1 and 14b-2, respectively, broker-dealers and banks must distribute certain materials received from an issuer or other soliciting party to their customers who are beneficial owners of securities of that issuer only if the broker-dealers and banks are

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[13] 17 CFR 240.14b-1(b); 17 CFR 240.14b-2(b).

[14] *See* Proxy Mechanics Concept Release, *supra* note 12, at 42999. Estimates of shares held by OBOs range from 52 to 60 percent of all shares. *Id.*

Rule 22c-2 under the Investment Company Act, which we adopted to help address abuses associated with short-term trading of fund shares, generally requires funds to enter into shareholder information agreements with certain intermediaries that submit orders to purchase or redeem fund shares on behalf of beneficial owners, but the rule and such agreements do not require the information that would be necessary to enable the fund to deliver or transmit materials directly to beneficial owners. 17 CFR 270.22c-2(a)(2)(i). These agreements provide the fund with certain limited information about transactions by beneficial owners whose shares are held in street name or "omnibus" accounts through those financial intermediaries. 17 CFR 270.22c-2(c)(5). However, the rule does not require this information provided under the terms of a shareholder information agreement to include, for example, the name and address of the beneficial owner. We excepted money market funds, funds that issue securities that are listed on a national securities exchange, and funds that affirmatively permit short-term trading of their securities from the requirements of 22c-2 unless they elect to impose a redemption fee under the rule. 17 CFR 270.22c-2(b).

[15] In the proxy context, these service providers are sometimes characterized as "proxy service providers." *See* 2013 Amendments Approval, *supra* note 8. Because the scope of this Request for Comment does not include delivery of fund proxy materials, we generally refer to this type of service provider as a "fulfillment service provider."

assured reimbursement of reasonable expenses, both direct and indirect, from the issuer. These rules provide that such materials may include proxy statements, information statements, annual reports, proxy cards, and other proxy soliciting materials.[16] In addition, NYSE rule 465 requires NYSE member firms to forward interim reports and other material being sent to stockholders by issuers if the member firm is assured it will be reimbursed for all out-of-pocket costs, including reasonable clerical expenses.[17] In the fund context, we understand that industry participants have used the framework established by the Exchange Act rules and NYSE rules to deliver materials including prospectuses, summary prospectuses, and annual and semiannual reports to investors.

In adopting our rules, we did not determine what constituted "reasonable expenses" that were eligible for reimbursement.[18] Rather, as discussed below, the rules of SROs set forth these amounts.[19] We believed at the time that SROs would be best positioned to make a fair evaluation and allocation of the costs associated with the distribution of shareholder materials.[20] Accordingly, it is the SRO rules that establish the maximum amount that an SRO member may receive for distributing materials to beneficial owners.

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[16] 17 CFR 240.14b-1(b); 17 CFR 240.14b-2(b).

[17] *See* NYSE rule 465 of listed company manual.

[18] Proxy Mechanics Concept Release, *supra* note 12, at 42995.

[19] *See, e.g.*, NYSE rule 451.90(3); Supplementary Material .01(a)(4) to FINRA rule 2251.

[20] *See* Order Granting Accelerated Approval to Amendment No. 1 to Proposed Rule Change Relating to a One-Year Pilot Program for Transmission of Proxy and Other Shareholder Communication Material, Exchange Act Release No. 38406 (Mar. 14, 1997) [62 FR 13922 (Mar. 24, 1997)]. This belief was in part attributed to SRO exchanges acting as "representatives of both issuers and brokers," however we recognize that FINRA, as the sole national securities association, has often led in promulgating fund-specific SRO rules in certain areas that govern broker-dealers. *See id.*; *infra* note 36 and accompanying text.

C. Current NYSE Regulation of Fees for Forwarding Fund Materials to Investors

Currently, NYSE rules 451 and 465 establish the fee structure for which an NYSE member organization may be reimbursed for expenses incurred in connection with the forwarding of certain issuer materials to investors. Under these rules, members may request reimbursement of expenses at less than the approved rates; however, no member may seek reimbursement at rates higher than the approved rates or for items or services not specifically listed without the prior notification to and consent of the issuer.[21] Issuers reimburse the vast majority of firms that distribute their material to investors at the NYSE fee schedule rates because the vast majority of the intermediaries are NYSE members or members of FINRA, which has a rule that is similar to the NYSE's rules.[22]

Currently, the NYSE rules set forth the following processing and other fees that are applied to the forwarding of Fund Materials:

- *Interim Report Fee.* A processing fee up to 15 cents for each account for fund annual reports processed separately from proxy materials, for "interim reports," and for "other material."[23] In the fund context, we understand that this rule has been interpreted to apply, for example, to each distribution of fund annual and semiannual reports, as well as annual mailings of summary prospectuses, statutory prospectuses, and other materials sent to investors that are not proxy distributions.

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[21] *See* NYSE Supplementary Material to rule 451.93. Since 1937, the NYSE has required issuers, as a matter of policy, to reimburse its members for out of pocket costs of forwarding materials. *See* Proxy Mechanics Concept Release, *supra* note 12, at 42995. Rules formally established reimbursement rates in 1952, and such rules have been revised periodically since then. *Id.*

[22] *See* Proxy Mechanics Concept Release, *supra* note 12, at 42995.

[23] *See* NYSE rule 451.90(3); Supplementary Material .01(a)(4) to FINRA rule 2251.

- *Preference Management Fee.* A fee of up to 10 cents per distribution of Fund Materials listed above for each "suppressed" account for which the intermediary has eliminated the need to send the materials in paper format through the mails.[24] This may include, for example, documents delivered electronically[25] and "householded" accounts where no distribution takes place.[26] This fee is in addition to, and not in lieu of, other fees permitted under the NYSE rule, including the interim report fee.[27] Thus, the aggregate processing fee for distributing Fund Materials to suppressed accounts is 25 cents per distribution (15 cents for an interim report fee plus 10 cents for a preference management fee).

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24 *See* NYSE rule 451.90(4); Supplementary Material .01(a)(5) to FINRA rule 2251. For additional discussion of the preference management fee, see *infra* Part III.D. The preference management fee is, however, higher—up to 32 cents—for certain proxy materials. NYSE rule 451.90(4).

25 *See, e.g.*, Use of Electronic Media for Delivery Purposes, Investment Company Act Release No. 21399 (Oct. 6, 1995) [60 FR 53458 (Oct. 13, 1995)] (providing Commission views on the use of electronic media to deliver information to investors, with a focus on electronic delivery of prospectuses, annual reports, and proxy solicitation materials); Use of Electronic Media by Broker-Dealers, Transfer Agents, and Investment Advisers for Delivery of Information, Investment Company Act Release No. 21945 (May 9, 1996) [61 FR 24644 (May 15, 1996)] (providing Commission views on electronic delivery of required information by broker-dealers, transfer agents, and investment advisers); Use of Electronic Media, Investment Company Act Release No. 24426 (Apr. 28, 2000) [65 FR 25843 (May 4, 2000)] (providing updated interpretive guidance on the use of electronic media to deliver documents on matters such as telephonic and global consent, issuer liability for website content, and legal principles that should be considered in conducting online offerings).

26 *See, e.g.,* rule 154 under the Securities Act of 1933 (permitting householding of prospectuses) [17 CFR 230.154]; rules 30e-1(f) and 30e-2(b) under the Investment Company Act (permitting householding of shareholder reports); rules 14a-3(e) and 14c-3(c) under the Exchange Act (permitting householding of annual reports to security holders, proxy statements and information statements, and Notices of Internet Availability of Proxy Statements) [17 CFR 240.14a-3(e); 17 CFR 240.14c-3(c)]. *See generally* Delivery of Disclosure Documents to Households, Investment Company Act Release No. 24123 (Nov. 4, 1999) [64 FR 62540 (Nov. 16, 1999)] (adopting householding rules with respect to prospectuses and shareholder reports); Delivery of Proxy Statements and Information Statements to Households, Investment Company Act Release No. 24715 (Oct. 27, 2000) [65 FR 65736 (Nov. 2, 2000)] (adopting householding rules with respect to proxy statements and information statements).

27 *See* NYSE rule 451.90(4); Supplementary Material .01(a)(5) to FINRA rule 2251.

- *Notice and Access Fee.* When a fund elects to send proxy materials via the notice and access method, the rules permit an additional notice and access fee.[28] The notice and access fee is a tiered fee based on the number of accounts per distribution with a schedule that begins at 25 cents per account and ultimately declines to 5 cents per account.[29] The Commission approved amendments specifying the applicability of notice and access fees to distributions of fund shareholder reports under Investment Company Act rule 30e-3.[30] For distribution of fund shareholder reports under rule 30e-3, an intermediary may not charge a notice and access fee for any account with respect to which a fund pays a preference management fee for the same distribution.[31]

In addition to the processing, preference management, and notice and access fees described above, the NYSE rules provide for reimbursement for actual postage costs, the actual cost of envelopes unless they are provided by the fund, and any actual communication expenses incurred in receiving voting returns (in the case of proxy distributions).

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28 *See* NYSE rule 451.90(5); Supplementary Material .01(a)(6) to FINRA rule 2251. The notice and access model for the delivery of proxy materials permits issuers to send investors a "notice of internet availability of proxy materials" in lieu of the traditional paper mailing of proxy materials. *See* 2013 Amendments Approval, *supra* note 15, at 63535.

29 *See* NYSE rule 451.90(5); Supplementary Material .01(a)(6) to FINRA rule 2251. Under the schedule, every fund will pay the highest rate (*i.e.*, 25 cents) for the first 10,000 accounts, or portion thereof, with decreasing rates applicable only on additional accounts in the additional tiers, with rates gradually falling to the fee of 5 cents for each account over 500,000 accounts. *See id.*

30 *See* Exchange Act Release Nos. 83378 (June 5, 2018) (Order Affirming Action by Delegated Authority Approving SR-NYSE-2016-55 and Discontinuing Stay); 79370 (Nov. 21, 2016) [81 FR 85655 (Nov. 28, 2016)] (Stay Order); 79355 (Nov. 18, 2016) [81 FR 85291 (Nov. 25, 2016)] (Approval Order) ("2016 Amendments Approval"); *supra* note 5. For purposes of calculating rates for distribution of fund shareholder reports under rule 30e-3, all accounts holding shares of any class of stock of the applicable fund are aggregated in determining the appropriate pricing tier. *See* NYSE rule 451.90(5).

31 *Id.*

The NYSE rules also provide for the form of a billing document to be used by its members to seek reimbursement.[32] For each category of distribution, such as "interim reports," the NYSE member specifies the number of reports mailed, the service fee, the number of envelopes not supplied by the issuer used, the U.S. postage, the foreign postage, the cost of mail, and the total cost assessed.

III. DISCUSSION AND REQUEST FOR COMMENT

A. General Framework

As discussed above, we are seeking public comment and additional data on the framework for fees charged by intermediaries for the distribution of shareholder reports and other Fund Materials to investors.

Request for Comment

- Should the current rules regulating processing fees for distributing materials to beneficial owners apply to forwarding Fund Materials? Do the differences between proxy distributions and non-proxy distributions create significant differences in the costs? Would considering those types of fees separately help improve the evaluation of what constitutes "reasonable expenses" in situations other than proxy distributions?
- Are our rules under Section 14 of the Exchange Act (*e.g.*, rules 14b-1 and 14b-2) well-tailored for the distribution of Fund Materials? Would additional or other Commission rules be preferable? If so, what should they provide? For example, should there be a different set of rules that applies to the distribution of all types of fund materials, including proxy materials? Should these rules apply only to certain materials such as shareholder reports and/or prospectuses?

[32] NYSE rule 465.30.

- We understand that processing fees and other expenses connected with distributing Fund Materials to investors are considered and treated as direct fund expenses. Is our understanding correct? If not, who pays these fees and expenses and under what circumstances? How are fund payments for forwarding material to beneficial shareholders different from similar payments made by operating companies? Are fund investors more directly affected by the payments than operating company investors?
- Is the current fee and remittance structure for the distribution of Fund Materials to investors reasonable? Should the fees be presented differently to better explain how they are applied and allow funds to verify that they are correct?
- Does the current fee framework encourage, discourage, or not affect fund communications with investors beyond those communications that are required?
- Do intermediaries and their agents provide funds with invoices for processing fees assessed on Fund Material distributions? If so, are they sufficiently detailed and transparent for the fund to be able to evaluate their accuracy and whether they have been assessed in a manner consistent with SRO rules? If such invoices are not sufficiently detailed or transparent, what additional information should be provided? Does a fund need information about any remittances that the fulfillment service provider will pay to the intermediary in connection with the services encompassed by the invoice?
- Do funds challenge fees assessed by intermediaries or their agents for distribution of Fund Materials on the basis that the fees are not reasonable? If so, under what circumstances? If not, what are the impediments, if any, to doing so? How, if at all, would withholding fees deemed to be unreasonable affect the fund or its investors?

- With what frequency do funds make requests for the names and addresses of NOBOs? What percentage of fund beneficial accounts are NOBO accounts? Would low percentages of NOBOs relative to all fund beneficial owners be a disincentive to use such lists? With what frequency do funds make such requests to facilitate the distribution of Fund Materials, or for other purposes? How can more direct communication between funds and NOBOs be facilitated? Do funds currently rely on intermediaries to forward materials to investors rather than requesting a list of NOBOs? Does the current NYSE NOBO fee structure discourage funds from directly sending Fund Materials to NOBOs?

B. SRO Rules

Although the NYSE's rules currently apply to the forwarding of Fund Materials to investors, the NYSE has observed that it "has no involvement in the mutual fund industry" and that it "may not be best positioned to take on the regulatory role in setting fees for mutual funds."[33] The NYSE and some commenters have recommended that FINRA should take on this role.[34] As noted above, FINRA has adopted rules that generally mirror the previously adopted NYSE rules.[35] FINRA also has adopted rules governing broker-dealers' sales practices and other conduct with respect to funds.[36]

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[33] 2016 Amendments Notice, *supra* note 5, at 56718.

[34] *Id.*; *see also* 2016 Ariel Letter, *supra* note 10; 2016 Columbia Letter, *supra* note 10; 2016 Dimensional Letter, *supra* note 10; 2016 Invesco Letter, *supra* note 10; 2016 ICI Comment Letter, *supra* note 4; 2016 ICI Letter II, *supra* note 10; 2016 MFS Letter, *supra* note 10; 2016 T. Rowe Letter, *supra* note 10.

[35] *Compare* FINRA rule 2251 *with* NYSE rule 451; *see supra* note 19 and accompanying text.

[36] For example, FINRA rules bar broker-dealers who are members from selling funds that impose combined sales charges that exceed certain limits, including "asset-based sales charges" and shareholder servicing fees. FINRA rule 2341; *see also* Mutual Fund Distribution Fees, Investment Company Act Release No. 29367 (July 21, 2010) [75 FR 47064, 47069 (Aug. 4, 2010)]. FINRA also requires the filing of certain fund advertising material. FINRA rule 2210.

Request for Comment

- Should FINRA be the SRO for setting the structure and level of processing fees for funds? If not, should another entity other than an SRO be responsible? If so, who?
- Are there particular areas of expertise such as funds' operations, distribution methods, and sales practices that would be most relevant in setting processing fees? If so, what expertise and does this expertise vary from one SRO to another?

C. Fulfillment Service Providers

We understand that while the fund typically pays the processing fees charged by a intermediary's fulfillment service provider, the fund has little or no control over the process by which the fulfillment service provider is selected, the terms of the contract between the intermediary and the service provider, or the fees that are ultimately incurred and billed for the distribution of Fund Materials to investors.[37]

It remains our understanding that the fulfillment service provider generally bills funds the maximum fees allowed by the NYSE rules, and in some cases, the fulfillment service provider is contractually *obligated* to its intermediary clients to do so. However, commenters have stated that the fees that the fulfillment service provider charges certain intermediary clients for its services sometimes are less than the fees charged to funds on the intermediaries' behalf. The result is a remittance or rebate from the fulfillment service provider to those intermediaries.[38]

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[37] *See* Proxy Mechanics Concept Release, *supra* note 12, at 42997.

[38] *See* 2013 ICI Letter, *supra* note 10; Comment Letter of the Securities Transfer Association (Mar. 4, 2013) on File No. SR-NYSE-2013-07, *available at* https://www.sec.gov/comments/sr-nyse-2013-07/nyse201307.shtml ("2013 STA Letter"); *but see* Comment Letter of Broadridge Financial Solutions (Sep. 12, 2106) on File No. SR-NYSE-2016-55, *available at* https://www.sec.gov/comments/sr-nyse-2016-55/nyse201655-8.pdf. Under rule 14b-1 under the Exchange Act, intermediaries are permitted to seek reimbursement of not only "direct" reasonable expenses but also "indirect" reasonable expenses. *See* 17 CFR 240.14b-1(c)(2)(i).

Some commenters have asserted that fees charged for distribution of materials to intermediated accounts "far exceed" the costs a fund incurs for distributing the same materials to investors whose shares are registered directly with the fund's transfer agent.[39]

We are interested in commenters' views on such remittance and rebate practices.

Request for Comment

- Is the current framework for the distribution of Fund Materials to fund investors—in which the fulfillment service provider is selected by an intermediary but costs incurred are paid by the fund—appropriate? Does the current framework encourage intermediaries to reduce costs for funds? Should funds have more control over the selection of, services billed to, and payments made to fulfillment service providers? What are the potential benefits and drawbacks of such alternatives?
- How do fees charged to funds on an intermediary's behalf for delivery of Fund Materials compare with fees negotiated for comparable services between funds and their service providers for distributions of similar materials to investors holding shares directly with the fund or NOBOs known to the fund? If they are different, are they higher or lower, and by how much? If they are different, why are they different? For example, are the services provided also different, such as in quality or complexity? If so, is the magnitude of the difference in processing methods or services provided commensurate with the difference in fees? Does the magnitude of the difference vary depending on the manner in which the materials are delivered, such as in paper through the mail, by electronic delivery, or through a notice and access system?

[39] *See supra* note 38.

- What factors may affect the level of competition in the market for fulfillment service providers and their fees? Does the presence or absence of competition affect the level of fees assessed or the size of remittances?
- What steps, if any, should the Commission take to promote competition in the market for the distribution of Fund Materials to investors?
- To what extent do intermediaries receive remittances or rebates from fulfillment service providers for non-proxy deliveries? What, if any, additional related costs do intermediaries incur in connection with non-proxy distributions? Do intermediaries and/or their fulfillment service providers inform funds as to the amounts and related costs and services associated with such remittances?

D. Preference Management Fee

Under the current framework, once a paper mailing is suppressed, the intermediary, or its agent, collects a preference management fee for each distribution of Fund Materials, even though the continuing role of the intermediary, or its agent, with respect to subsequent delivery of documents to investors, is limited to keeping track of the investor's election. While corporate issuers typically only incur this fee annually in connection with soliciting proxies for their annual meeting, funds often pay this fee multiple times per year for the distribution of a fund's annual and semiannual reports to shareholders, prospectuses, and other Fund Materials.

We understand that tracking an investor's preferences or elections typically occurs at the account level for all securities held for all types of issuers. The elections, moreover, may also apply to other customer communications, including account statements, confirmation statements, tax documents, and other materials. The costs of maintaining customer elections for those latter materials would not generally be subject to reimbursement by issuers under Exchange Act rules

14b-1 and 14b-2 and NYSE rules 451 and 465, but would instead be borne by the intermediaries themselves.[40] In addition, we understand that this fee is applied for each distribution of Fund Materials, not only where the need to send materials in paper format has been eliminated due to the procurement by the intermediary of affirmative consent to electronic delivery of those materials, but also when our rules concerning "householding" are relied upon.

Request for Comment[41]

- Should the application of the preference management fee for Fund Materials be eliminated on an ongoing basis once an investor elects electronic delivery? Should the fee continue to be permitted to be assessed on a per-distribution basis or with some other frequency, such as annually? How often does a typical investor change a delivery preference once paper deliveries have stopped with respect to that investor? Do delivery preferences depend on type of document? Does the difference in frequency between proxy deliveries and non-proxy deliveries justify separating preference management fees for forwarding of proxy materials from preference management fees for forwarding non-proxy materials?
- How, if at all, does the application of the preference management fee affect overall electronic delivery rates for Fund Materials distributions? How, if at all, does it affect the level of processing fees and aggregate costs that funds pay? Is it appropriate that aggregate processing fees (exclusive of expenses such as printing and mailing) are greater

[40] Rules 14b-1 and 14b-2 also do not require reasonable reimbursement for activities related to sending these materials.

[41] None of the questions in this release should be interpreted to reflect any conclusion regarding the appropriate role, if any, of the Commission in setting fees in this area.

for Fund Materials that are "suppressed" (*e.g.*, sent by email or not sent at all in the case of householded accounts) than for those delivered in paper?

- What proportion of the total expense of maintaining delivery preference elections is reimbursed by issuers in the context of individual distributions of forwarded materials? What proportion of those total expenses does the securities intermediary bear in the course of sending its own materials to its customers? Are those proportions commensurate with the effort and expense involved in carrying out each type of distribution?
- Compared with other issuers, do funds pay more in preference management fees on either a per-account or per-distribution basis? If so, why?

E. Processing Fees to Managed Accounts

For certain "managed accounts," the processing fees are assessed for all accounts, even though the fund materials are only required to be distributed to the investment manager.[42] The NYSE rules apply a smaller preference management fee for distributions of certain proxy materials to managed accounts than they do to other types of intermediated accounts. Also, the rules prohibit the application of any fees, including a preference management fee, for managed accounts with five or fewer shares.[43]

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[42] *See* Proxy Mechanics Concept Release. The NYSE rules provide that, for this purpose a "managed account" "shall mean an account at [an intermediary] which is invested in a portfolio of securities selected by a professional advisor, and for which the account holder is charged a separate asset-based fee for a range of services which may include ongoing advice, custody[,] and execution services." *See* NYSE rule 451.90(6).

[43] The preference management fee, which is otherwise permitted to be up to 32 cents for each such distribution per "suppressed" account, is 16 cents instead. NYSE rule 451.90(4). The preference management fee for distributing interim reports, annual reports mailed separately and other material is 10 cents irrespective of whether it is being charged for a regular account or a managed account.

Request for Comment

- How are processing fees for Fund Materials assessed with respect to managed accounts? Should certain kinds of accounts, such as separately managed accounts, where multiple investors may delegate their investment decisions to a single investment manager, be eligible for further different treatment under the current fee structure? If so, why and how should they be treated differently?
- Is the current application of processing fees for distributions of Fund Materials to managed account investors appropriate? Should such distributions to managed accounts be charged at a reduced rate as they are in the proxy distribution context?[44] If so, what rate?
- What services do intermediaries or fulfillment service providers typically provide to managed account investors?

F. Other Arrangements Between a Fund and Intermediary

As discussed above, unlike in the operating company context, a "securities intermediary" through which shares are held in street name is also generally a "financial intermediary" under Investment Company Act rule 22c-2. Therefore, a fund is required to contract with the financial intermediary to share information about the submission of purchase and redemption orders.[45] In some cases, financial intermediaries may enter into "sub-transfer agent" or "sub-accounting" servicing arrangements with funds to provide administrative or shareholder services to investors

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[44] *See id.*

[45] *See supra* note 12. *See* rule 22c-2 under the Investment Company Act [17 CFR 270.22c-2] (permitting certain funds to impose redemption fees for holders redeeming securities within seven calendar days after purchase). We understand, however, that certain funds whose shares are traded in the secondary market, such as exchange-traded funds and closed-end funds, may be intermediated in the same manner as operating companies and thus do not have the same contractual relationships with the intermediary that many open-end funds do.

whose shares are held in "omnibus accounts." Many funds also have "selling" agreements with certain intermediaries for the distribution of fund shares.[46] An operating company, by contrast, may have no direct relationship with the intermediary. Some commenters have questioned whether fund payments under the SRO rules may be duplicative of payments made for similar services under contractual arrangements between a fund and an intermediary.[47]

Request for Comment

- Do funds present facts and circumstances that merit differentiating them from other types of issuers as to appropriate levels of processing fees for the distribution of Fund Materials to beneficial owners? How, if at all, are fund payments to intermediaries pursuant to plans adopted by funds pursuant to rule 12b-1 under the Investment Company Act ("12b-1 plans"), shareholder service agreements, or other similar arrangements with intermediaries relevant considerations in differentiating Fund Material distributions from distributions of operating company materials?
- Does this framework result in duplicative payments from a fund to an intermediary for the same services? Does the presence of any such arrangement bear on the appropriateness of the practice of paying remittances?
- Do operating companies have arrangements with intermediaries similar to agreements related to 12b-1 plans?

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[46] *See generally* Division of Investment Management Guidance Update No. 2016-01 (Jan. 2016) (discussing mutual fund distribution and sub-accounting fees); rule 12b-1 under the Investment Company Act [17 CFR 270.12b-1].

[47] *See, e.g.*, 2013 ICI Letter, *supra* note 10 (questioning, "for example, the extent to which preference management fees might be duplicative in light of contractual arrangements between [funds] and broker-dealers holding street name accounts that already provide for compensation to the broker-dealer to maintain distribution preferences").

- How does the presence of sub-transfer agent, sub-accounting, or selling arrangements affect the appropriateness of the payment of a preference management fee or notice and access fees? Are such payments duplicative?
- Would some funds be more adversely impacted by potential fee duplication than others?
- Are the costs of distributing shareholder reports and other materials to fund investors covered by administrative services, recordkeeping, or other similar contractual arrangements? If the fee schedule did not apply in such cases, would the costs of distributing Fund Materials to fund investors increase or decrease? Why?

IV. GENERAL REQUEST FOR COMMENT

This request for comment is not intended to limit the scope of comments, views, issues, or approaches to be considered. In addition to investors and funds, we welcome comment from other market participants and particularly welcome statistical, empirical, and other data from commenters that may support their views or support or refute the views or issues raised by other commenters.

By the Commission.

Dated: June 5, 2018

Brent J. Fields
Secretary