IDC
INDEPENDENT DIRECTORS COUNCIL
Committed to Strong Fund Governance

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October 31, 2018

Mr. Brent Fields
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549-1090

Re: Request for Comments on the Processing Fees Charged by Intermediaries for Distributing Materials Other Than Proxy Materials to Fund Investors; File No. S7-13-18

Dear Mr. Fields:

The Independent Directors Council[1] appreciates the opportunity to comment on the framework under which intermediaries charge processing fees for distributing certain non-proxy disclosure materials to fund investors, such as shareholder reports and prospectuses ("fund materials").[2] Fund directors oversee fund expenses on behalf of fund shareholders and therefore have a strong interest in ensuring that these processing fees, which are ultimately borne by fund shareholders, are fair and reasonable. We are concerned that the current framework for these fees creates a conflict of interest that results in artificially higher costs for delivering fund materials to shareholders.[3] Thus, we commend the Commission for addressing this issue.

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[1] The Independent Directors Council serves the US-registered fund independent director community by advancing the education, communication, and policy positions of fund independent directors, and promoting public understanding of their role. IDC's activities are led by a Governing Council of independent directors of Investment Company Institute member funds. ICI is the leading association representing regulated funds globally, including mutual funds, exchange-traded funds, closed-end funds, and unit investment trusts in the United States, and similar funds offered to investors in jurisdictions worldwide. ICI's members manage total assets of US$22.7 trillion in the United States, serving more than 100 million US shareholders, and US$7.3 trillion in assets in other jurisdictions. There are approximately 1,700 independent directors of ICI-member funds. The views expressed by IDC in this letter do not purport to reflect the views of all fund independent directors.

[2] *See* Request for Comments on the Processing Fees Charged by Intermediaries for Distributing Materials Other Than Proxy Materials to Fund Investors, SEC Rel. Nos. 33-10505; 34-83379; IC-33114 (June 5, 2018) (the "Release").

[3] IDC previously voiced concern regarding processing fees in the context of proxy materials. *See* Letter from Dorothy A. Berry, Chair, IDC Governing Council, to Elizabeth M. Murphy, Secretary, U.S. Securities and Exchange Commission, dated October 20, 2010, available at https://www.sec.gov/comments/s7-14-10/s71410-158.pdf (noting the lack of incentive for intermediaries or proxy service firms to reduce their processing fees or provide cost-efficient services and the reduced returns for shareholders due to processing fees that are passed on as a fund expense). Although the scope of the

Under the current framework, the fund's intermediary, which is typically selected by the shareholder, selects a vendor to forward fund materials to investors who hold shares of the fund through that intermediary. The intermediary negotiates the price with the vendor, and the vendor bills the fund for delivery of the fund materials. A fee schedule contained in the New York Stock Exchange Rules sets forth the maximum rates that an intermediary can reasonably charge a fund for reimbursement. It is common practice for the vendor to charge the maximum allowable rate to the fund, and then to rebate a portion of the payment to the intermediary. Under this structure, the intermediary has no incentive to negotiate a competitive fee for the benefit of shareholders and the fund has no choice but to pay the vendor's bill as presented. We do not believe intermediaries disclose these fees to their customers.

This disconnect between who negotiates the price and who pays also presents an obstacle to market forces, creating an environment for a single dominant vendor to thrive financially at the expense of fund shareholders. A recent ICI survey found that the cost of delivering fund materials to shareholders who invest directly with the fund is significantly less than the rates charged under the NYSE fee schedule.[4] For example, the survey found that a fund typically pays three times as much in processing fees for mailing the same shareholder report to an intermediary-held account as compared to an account held directly with the fund. That differential increases to five times as much for a shareholder report that is emailed (or "suppressed"). This striking disparity in fees shows that the rates set forth in the NYSE fee schedule do not represent "reasonable" fees, and that vendors are willing and able to negotiate fees to deliver fund materials for significantly less than the rates set forth in the NYSE fee schedule.

Directors are concerned that the current structure is not formulated in the best interests of fund shareholders.[5] In order to resolve the inherent conflict of interest and foster competition in the market, IDC strongly recommends that the Commission allow funds themselves to select the vendor and negotiate the processing fees they pay.[6] If the SEC overhauls the existing framework to eliminate the conflict of interest, then market competition will establish the fees and there will be no need for the

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Commission's request for comment does not include the processing fees for delivery of proxy materials to beneficial owners of fund shares, we urge the Commission to undertake a similar examination of the framework for those fees. Our comments herein would apply equally in that context as well.

[4] ICI's survey consists of data gathered data from 1,704 mutual funds from 50 of its members. Collectively, these members have 2,901 mutual funds that total $7.3 trillion in assets under management as of August 2018.

[5] The NYSE fee schedule is not suited for the distribution of fund materials. Indeed, the Release notes that the current framework was designed primarily for operating company proxy materials. Release at 4.

[6] We note that ICI also recommends the SEC realign the disconnect between who negotiates and who pays. ICI recommends that if the SEC chooses to retain the existing fee framework, however, then the fee schedule must be reworked to create a different and separate set of rules (apart from that of operating companies) to reflect the actual cost of forwarding fund materials to beneficial owners. *See* Letter from Susan Olson, ICI General Counsel, to Mr. Brent J. Fields, Secretary, U.S. Securities and Exchange Commission, dated October 31, 2018. IDC agrees with that recommendation.

current regulator set fee schedule. This "realignment" also would force vendors to compete on cost, with funds seeking the best price and service for their shareholders.

If you have any questions about our comments, please contact me at [redacted].

Sincerely,

Amy Lancellotta

Amy B.R. Lancellotta
Managing Director

cc: The Honorable Jay Clayton
The Honorable Kara M. Stein
The Honorable Robert J. Jackson Jr.
The Honorable Hester M. Peirce
The Honorable Elad L. Roisman

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