MEMORANDUM

TO: Public Comment File No. S7-27-03

FROM: Penelope W. Saltzman
Office of Regulatory Policy
Division of Investment Management

DATE: November 18, 2004

On November 11, 2004, representatives of The SPARK Institute, Inc. ("SPARK"), Wachovia Corporation ("Wachovia"), and the United States Postal Service ("USPS") met with staff 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 from the Division of Investment Management attended the meeting: Robert Plaze, Associate Director, and Penelope Saltzman, Branch Chief.

The representatives discussed aspects of (i) the alternative approach to the Late Trading Proposal described in SPARK's comment letter and (ii) a new concept related to the approach. The alternative approach would allow intermediaries to obtain same-day pricing for orders they receive by 4 p.m. and transmit to fund companies after 4 p.m. as long as the intermediary meets specific requirements, as described in the documents attached to the memorandum to this file dated August 19, 2004. The new concept would involve the application of a sequence number to each set of instructions entered into a fund intermediary's trade processing system, as described in the document attached to the memorandum to this file dated October 21, 2004.[1]

Representatives from USPS discussed the time-stamp technology that is part of the USPS electronic postmark, which is described in the USPS comment letter. The representatives also described the additional application of transaction number sequencing. In response to questions from Commission staff, the representatives assured the staff that other private companies that have developed time stamp technology also are working on incorporating transaction number sequencing in that technology. Representatives from SPARK and Wachovia discussed ways in which the transaction number sequence concept would be applied in the order processing system.

In addition to this meeting, representatives from SPARK have responded in writing to questions staff posed regarding the alternative approach, including transaction number sequencing. The response is attached.

Attachment

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[1] Representatives of SPARK and Wachovia first discussed their alternative approach with staff members at a meeting on April 14, 2004, and first discussed the new concept at a meeting on October 20, 2004.

THE
SPARK
Institute, Inc.

Glenna S. Best
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November 5, 2004

Penelope Saltzman
Branch Chief, Office of Regulatory Policy
Division of Investment Management
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549

Re: Sequential Numbering Enhancement

Dear Penelope:

Thank you for allowing the SPARK Institute the opportunity to respond to your additional questions about the SPARK Solution alternative to proposed rule amendments concerning the pricing of investment company shares and the sequential numbering enhancement to the SPARK Solution. We believe that this technological enhancement would provide an important additional safeguard against potential late trading abuse by enabling mutual fund transfer agents (or their agents, such as Fund/SERV) to monitor whether all instructions processed by a retirement plan recordkeeper or other intermediary are received by 4 p.m. on a "real-time" basis. Specifically, this letter follows up on two questions raised in our discussions. For convenience, capitalized terms have the meaning described under the Draft Criteria for Financial Intermediaries Performing After Hours Trade Processing (dated July 30, 2004) (the "Criteria").

First, you asked about the operation of sections 1.9.6 and 1.9.7 of the Criteria. Under those sections, generally, certain types of Instructions can be treated as also including an Instruction to trade a "lesser included" amount where the application of Price information in processing the Instruction would make the Instruction impossible to implement (i.e., as a result of a decline share price, a participant's account does not have sufficient fund shares to satisfy a fixed dollar amount redemption, loan or similar instruction, or plan rules or ERISA restrict liquidation of a portion of the participant's account). Under this approach, certain Instructions or Orders may be modified after the 4 p.m. eastern time "Pricing Time" and will not be treated as "corrections" for purposes of the Criteria. The Criteria would allow an Intermediary to treat an Instruction as an

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Instruction with respect to a "lesser included" amount only if the Intermediary's after hours trade processing system "can maintain an audit trail showing how the application of Price information impacts the Instruction and the Order."

You specifically asked whether a trade processing system would default to a lesser included amount under sections 1.9.6 and 1.9.7 automatically, or whether there is human intervention in the process. This depends on the features of each Intermediary's trade processing system. Some Intermediaries may program their trade processing systems to automatically apply these controls without any human intervention, or they may program their systems to automatically limit instructions in a way that generally avoids the types of issues addressed by sections 1.9.6 and 1.9.7. Other Intermediaries' trade processing systems may identify situations of the type described by sections 1.9.6 and 1.9.7, but a system operator must review and approve modification of the Instruction to the lesser included amount. However, in both situations, no modification of an Instruction or Order would be permitted unless the Intermediary's Trade Processing System can maintain an audit trail showing how the application of Price information impacted the Instruction and resulting Order.

Second, I would like to respond to your question about whether a recordkeeper could possibly construct a parallel order processing system on which instructions would not be assigned Transaction Sequence Numbers (TSNs), and then aggregate those instructions (possibly including instructions received after market close at 4 p.m.) with Instructions that are assigned valid TSNs as a way to cheat the system. Other criteria under the SPARK Solution would make this impossible. Specifically, section 4.2 of the Criteria provides that any Instructions effected in after hours trade processing must be automatically time stamped at point of entry to the after hours Trade Processing System that submits Orders to Funds. This means that any Instructions from a parallel recordkeeping system automatically would be time stamped and assigned TSNs when those Instructions are entered onto the after hours Trade Processing System that submits Orders to Funds. Also, section 4.6 of the Criteria provides that the Trade Processing System must be programmed so that only valid Instructions (i.e., bearing a valid TSN and timestamp within the appropriate time period) are included in Orders submitted in after hours trade processing on a business day. This control would prevent the aggregation of Instructions without valid TSNs submitted by a parallel order processing system with Instructions that have a valid TSN on the after hours Trade Processing System that submits orders to Funds.

I hope that this information is helpful. Please feel free to call me, or to contact Steve Saxon or Roberta Ufford of the Groom Law Group, Chartered, if you have further questions.

Very truly yours,

Bob

Robert G. Wuelfing
SPARK Institute

cc: Robert Plaze, Associate Director
C. Hunter Jones, Assistant Director
Adam Glazer, Attorney