INVESTMENT COMPANY INSTITUTE

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Comment Letter on NASD Proposal Regarding Nonelectronic Public Correspondence, September 1998

September 24, 1998

Mr. Jonathan G. Katz
Secretary
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549

Re: Proposed Rule Change by NASD Relating to Supervision of Correspondence (File No. SR-NASD-98-52)

Dear Mr. Katz:

The Investment Company Institute appreciates[1] the opportunity to comment on the National Association of Securities Dealers, Inc.'s ("NASD") proposed amendment to NASD Rule 3010 relating to the supervision of correspondence (the "Proposal").[2] The Proposal would require NASD members to review incoming non-electronic correspondence directed to registered representatives to properly identify and handle customer complaints and funds. As we indicated in our letter of May 12, 1998,[3] the Proposal, if implemented, would be extremely costly and burdensome to members without any corresponding benefits to investors. Accordingly, the Proposal should not be adopted, or at the very least, should be revised to allow more flexible procedures for addressing such correspondence.

Under the Proposal, for the first time, members would be required to review incoming non-electronic correspondence directed to registered representatives for purposes of properly identifying and handling customer complaints and funds. Where a member's office structure permits review of all correspondence, members would be required to designate a registered or associated person to open and review correspondence. The designated person could not be supervised or under the control of the representative whose correspondence is being reviewed. Where a member's office structure does not permit this arrangement, the firm would have to employ alternative procedures reasonably designed to assure adequate handling of complaints and checks. The Release provides specific examples of procedures that could be adopted in satisfaction of this requirement, such as forwarding correspondence to a member's Office of Supervisory Jurisdiction or branch manager for weekly review.

As we indicated in the May 12 Letter, the Proposal is entirely unnecessary to address any perceived problems with respect to written correspondence directed to registered representatives, since existing rules sufficiently address these matters. Rule 3010 already requires a member to develop written procedures that are appropriate to its business, size, structure, and customers for the review of incoming and outgoing written and electronic correspondence with the public relating to its investment banking or securities business.[4] Member firms also are required under Rules 3070(a)(2) and (c) and 3110(d) to review and report to the NASD customer complaints and keep detailed records of all customer complaints received in either electronic or non-electronic form. Although member firms may not necessarily review each and every piece of correspondence, they are required to develop policies to ensure that registered representatives and other employees use correspondence appropriately.

The Proposal lacks this flexibility and logic, since it would require review of every piece of incoming written correspondence directed to a registered representative so long as such review is possible. If a member's structure does not permit such review, detailed procedures along the lines described by the NASD in the Release would have to be adopted. Because existing NASD rules already address these issues, the Proposal should not be adopted.

If the Commission is nonetheless inclined to approve the Proposal, it should be revised to allow greater flexibility. We have two specific changes that should be made to the Proposal to accomplish this result.

First, the Proposal should not automatically require review of all incoming written correspondence directed to registered representatives, even if a member's business structure permits such review. Rather, a member should have the flexibility to design procedures to properly identify customer complaints and funds that best fit its business, size, structure, and customers (including consideration of whether the member firm's customers are institutional or retail), regardless of whether review of all incoming written correspondence is theoretically possible. This approach is more consistent with the original philosophy of the recent amendments to Rule 3010 regarding supervision and review of correspondence.

Second, the rule should specify that if a member does not normally receive written correspondence directed to registered representatives, the member is not required to develop procedures to address such correspondence. For example, NASD members that only serve as principal underwriters of mutual funds normally do not receive correspondence directed to individual registered representatives. A mutual fund's customer correspondence typically is directed to its transfer agent, and if the fund's underwriter does receive customer correspondence, it normally is not directed to a particular individual. These types of members should not have to develop procedures to address situations that they normally do not face.

We appreciate the opportunity to comment on the Proposal. If you have any questions, please contact me at (202) 326-5819.

Sincerely,

Joseph P. Savage
Assistant Counsel

cc: Katherine England
Mignon McLemore
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Securities and Exchange Commission

Mary Revell
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NASD Regulation, Inc.

ENDNOTES

[1] The Investment Company Institute is the national association of the American investment company industry. Its membership includes 7,288 open-end investment companies ("mutual funds"), 450 closed-end investment companies, and 9 sponsors of unit investment trusts. Its mutual fund members have assets of about $5.092 trillion, accounting for approximately 95% of total industry assets, and have over 62 million individual shareholders.

[2] Securities and Exchange Commission Release No. 34-40372 (Aug. 27, 1998), 63 Fed. Reg. 47059 (Sept. 3, 1998) (the "Release").

[3] See Letter from Joseph P. Savage, Assistant Counsel, Investment Company Institute, to Jonathan G. Katz, Secretary, Securities and Exchange Commission (May 12, 1998) (the "May 12 Letter").

[4] A member must, among other things, identify how supervisory reviews will be conducted and documented, identify what types of correspondence will be pre- and post-reviewed, identify what positions within the firm will be responsible for review of correspondence, specify the minimum frequency of reviews, monitor the implementation and compliance with the policies, and periodically re-evaluate the effectiveness of the firm's policies and procedures. See NASD Notice to Members 98-11 (Jan. 1998).