

Feds Dig for Disguised Fund Distribution Fees

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A nearly two-year SEC sweep examination of mutual funds' payments for distribution and other services appears to have concluded. Now, the question is what, if any, enforcement or other action the SEC will take. Mutual funds can make expenditures that are primarily intended to promote the distribution of fund shares only pursuant to written "Rule 12b-1" plans. However, when investors purchase mutual fund shares through broker-dealers and other intermediaries that use "omnibus accounts" and provide administrative services to the funds (e.g., "sub-transfer agent services"), a question arises whether any payments the funds make to the intermediaries are for distribution services, administrative services, or partially for each. In a 1998 letter to the Investment Company Institute, SEC staff discussed payments that mutual funds make, either directly or through their investment advisers, to "mutual fund supermarket" intermediaries. The letter warned fund boards to monitor to determine that any such payments that a fund considers to be for non-distribution services (and thus are not paid pursuant to a Rule 12b-1 plan) are reasonable in relation to the value of those services to the fund and its shareholders. **More recently, under the heading "Payments for Distribution in Guise," the SEC's published 2013 and 2014 examination priorities focused on "the wide variety of payments" made to intermediaries.** The SEC also recently expressed concern that the 1998 letter's guidance is not being followed. Accordingly, mutual funds would be well advised to consider whether all of their payments to intermediaries, and related disclosures are consistent with Rule 12b-1 and applicable guidance.

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