

MEMO# 12391

July 26, 2000

SEC PUBLISHES FOR COMMENT PROPOSED REVISIONS TO THE NASDR RULE GOVERNING PERFORMANCE FEE ARRANGEMENTS

[12391] July 26, 2000 TO: INVESTMENT ADVISERS COMMITTEE No. 20-00 SEC RULES COMMITTEE No. 99-00 RE: SEC PUBLISHES FOR COMMENT PROPOSED REVISIONS TO THE NASDR RULE GOVERNING PERFORMANCE FEE ARRANGEMENTS The Securities and Exchange Commission has published for comment revisions proposed by NASDR Regulation, Inc. ("NASDR") to Rule 2330 of the NASD Rules of Conduct, relating to transactions with customers. Currently, Rule 2330 permits a member of NASDR to receive compensation based on a share in profits or gains in a customer account if various specified conditions are satisfied. Prior to the SEC's revisions to Rule 205-3 under the Investment Advisers Act of 1940, which governs performance fee arrangements by investment advisers, the conditions set forth in Rule 2330 tracked those of Rule 205-3. Since the SEC amended Rule 205-3 in August 1998, however, the conditions of Rule 2330 have not been consistent with those of Rule 205-3. The NASDR's rule proposal is intended to address this inconsistency. In particular, NASDR has proposed to eliminate from the rule specific conditions and replace such conditions with a requirement that the member comply with "the conditions set forth in any applicable rule promulgated by the Commission." By amending Rule 2330 in this manner, NASDR hopes to ensure that the August 1998 amendments to Rule 205-3, as well as any future amendments to the rule, are incorporated into Rule 2330. Importantly, the SEC's Release also notes that it is the position of the SEC Division of Investment Management "that compensation received by a member or person associated with a member under [Rule 2330] would constitute 'special compensation' for purposes of the broker/dealer exception to the definition of 'investment adviser' in Section 202(a)(11)(C) of the Investment Advisers Act." As proposed, this position of the Division would be incorporated by footnote into the text of Rule 2330. A copy of the SEC's proposal is attached. Comments on the proposal are due to the Commission no later than August 11, 2000. If you have comments you would like the Institute to consider including in a possible comment letter, please submit them to Tamara Reed by phone (202-326-5825), fax (202-326-5839) or e-mail (tamara@ici.org) no later than Friday, August 4, 2000. Tamara Reed Associate Counsel Attachment Attachment (in .pdf format) 2

should not be considered a substitute for, legal advice.