INVESTMENT COMPANY INSTITUTE

MEMO# 10494

November 18, 1998

DRAFT INSTITUTE COMMENT LETTER ON NASD BOND FUND VOLATILITY RATINGS PROPOSAL

* See Memorandum to Advertising Subcommittee No. 44-98, SEC Rules Committee No. 113-98 and Unit Investment Trust Committee No. 34-98, dated November 10, 1998. [10494] November 18, 1998 TO: ADVERTISING COMPLIANCE SUBCOMMITTEE No. 47-98 SEC RULES COMMITTEE No. 118-98 UNIT INVESTMENT TRUST COMMITTEE No. 36-98 RE: DRAFT INSTITUTE COMMENT LETTER ON NASD BOND FUND VOLATILITY RATINGS PROPOSAL ____ As we previously reported, the Securities and Exchange Commission recently published for comment proposed changes to the National Association of Securities Dealers, Inc. rules that would permit, on an interim 18-month basis, brokerage firms to use bond fund volatility ratings in supplemental sales literature.* Attached and summarized below is the Institute's draft comment letter on this proposal. The letter states that the proposal addresses many, but not all, of the ICI's concerns about the use of "risk" ratings. The letter expresses general support for the proposal, subject to the proposal not being modified in any way that would weaken its investor protection provisions. In addition, the Institute's support is conditioned on the SEC and NASD undertaking a comprehensive review of the proposal at the end of the 18-month pilot period before determining whether to allow volatility ratings in supplemental sales literature on a permanent basis. The letter supports many of the conditions contained in the proposal, including the requirements that ratings be based exclusively on objective, quantifiable factors, and that ratings not be designated by a single symbol, letter or number. The letter also supports the requirement that ratings be current as of the most recent calendar quarter end as well as the proposal's disclosure requirements. The letter argues that the proposal should be modified, however, to prohibit the use of ratings that have been requested and paid for by a rated fund, since such arrangements raise inherent conflicts of interest that cannot be cured through disclosure. Comments on the proposal are due to the SEC no later than Monday, November 30, 1998. If you have comments on the Institute's comment letter, please contact Amy Lancellotta (telephone: 202/326-5824, fax: 202/326-5827, or e-mail: amy@ici.org) or the undersigned (telephone: 202/326-5819) no later than Wednesday, November 25, 1998. Joseph P. Savage Associate Counsel Attachment

should not be considered a substitute for, legal advice.