INVESTMENT COMPANY INSTITUTE

MEMO# 5848

May 5, 1994

PROPOSED STATEMENT OF POSITION ON ENHANCED 12B-1 PLANS

May 5, 1994 TO: ACCOUNTING/TREASURERS COMMITTEE NO. 21-94 INDEPENDENT ACCOUNTANTS ADV. GROUP NO. 3-94 RE: PROPOSED STATEMENT OF POSITION ON ENHANCED 12B-1 PLANS ____ Enclosed for your review is a proposed exposure draft relating to enhanced 12b-1 plans. The proposed Statement of Position (SOP) Accounting for Certain Distribution Costs for Investment Companies was prepared by the Investment Companies Committee of the AICPA and issued for public comment on April 22. Traditional 12b-1 reimbursement plans provide that 12b-1 payments from the fund to the distributor are limited to actual costs incurred by the distributor. To the extent distribution costs incurred by the distributor exceed the maximum annual payment by the fund (e.g. 0.75%) the distributor may seek reimbursement in subsequent years. These "excess costs" are not treated as a liability by the fund since either fund shareholders or the Board may terminate the 12b-1 plan at any time. If the 12b-1 plan is terminated, the fund would have no obligation to reimburse the distributor for any remaining excess costs. Enhanced 12b-1 plans are similar to traditional 12b-1 reimbursement plans except that the plan provides that, in the event the plan is terminated for any reason, the fund would be required to reimburse the distributor for any remaining excess costs. Currently, excess costs are not treated as liabilities by funds with enhanced 12b-1 plans. The proposed SOP would require funds with enhanced 12b-1 plans to recognize a liability and an expense when distribution costs are incurred by the distributor. The amount of the liability would be equal to the cumulative costs incurred by the distributor less the sum of (a) cumulative 12b-1 fees paid to date, (b) cumulative CDSL payments to date and (c) if reasonably estimable, future cumulative CDSL payments by current shareholders. In calculating the liability, any future CDSL payments should be based on a) current net asset value per share, b) the number and aging of current shares outstanding, and c) the length of time a shareholder typically owns fund shares based on historical fund data or, if historical fund data are not available, group or industry data for a similar class of shares. The liability may be discounted to its present value if a) the amount and timing of cash flows are reliably determinable and b) the distribution costs are not subject to an interest charge. If these conditions are not met, the liability should be calculated without discounting to its present value. In addition, the proposed SOP would stipulate that if a traditional reimbursement plan is terminated and the board determines that the fund should reimburse the distributor for any excess costs, such excess costs be recognized as a liability by the fund when the board commits to pay such costs. Also, the proposed SOP would require funds to disclose in the footnotes to the financial statements the principal terms of both traditional and enhanced 12b-1 plans, including provisions permitting or requiring payment of excess distribution costs after plan termination. The SOP would also require disclosure of the aggregate dollar amount of excess distribution costs subject to recovery through future 12b-1 payments by the fund. The proposed SOP would be effective for annual financial statements for fiscal years beginning after December 15, 1994, and for interim statements for periods in such years. Comments on the proposed SOP are due to the AICPA on July 22, 1994. Please provide the undersigned with any comments you which to have included in the Institute's response to the AICPA on the proposed enhanced 12b-1 plan SOP by July 8. Gregory M. Smith Director - Operations/Compliance enclosure

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