

MEMO# 16861

December 9, 2003

NASD PROPOSAL TO REQUIRE EXPENSE RATIOS IN INVESTMENT COMPANY PERFORMANCE ADVERTISING; DEC. 17TH CONFERENCE CALL SCHEDULED

[16861] December 9, 2003 TO: ADVERTISING COMPLIANCE ADVISORY COMMITTEE No. 14-03 SEC RULES COMMITTEE No. 100-03 SMALL FUNDS COMMITTEE No. 32-03 UNIT INVESTMENT TRUST COMMITTEE No. 23-03 RE: NASD PROPOSAL TO REQUIRE EXPENSE RATIOS IN INVESTMENT COMPANY PERFORMANCE ADVERTISING; DEC. 17TH CONFERENCE CALL SCHEDULED The NASD has issued Notice to Members 03-77 seeking comment on a proposal to amend NASD Rule 2210, relating to communications with the public, and NASD Rule 2211, relating to institutional sales material, to require the disclosure of mutual fund expense ratios in performance advertising.¹ The NASD's proposal is summarized below. Comments on the proposal must be filed with the NASD by Friday, January 23, 2004. The Institute will hold a conference call on Wednesday, Dec. 17th at 3:00 p.m. EST to discuss the proposed amendments. The dial-in number for the call is 888-566-5778, and the pass code is 45976. If you plan to participate in the call, please send an e-mail to Monica Carter-Johnson at mcarter@ici.org. If you are unable to participate in the call, before the call please provide your comments on the proposed amendments to either Dorothy Donohue [(p) 202-218-3563; (f) 202-326-5839; (e-mail) Donohue@ici.org], or to Tamara Salmon [(p) 202-326-5825; (f) 202-326-5839; (e-mail) tamara@ici.org]. THE PROPOSED RULE REVISIONS As proposed, a new subsection (d)(3) would be added to Rule 2210 to require any communication with the public that includes investment company performance data as permitted by Rule 482 under the Securities Act of 1933 and Rule 34b-1 under the Investment Company Act of 1940 to disclose: (1) The standardized performance information mandated by Rules 482 and 34b-1; 1 See NASD Notice to Members 03-77 (Dec. 2003) (the "Notice"), which may be found on the NASD's website at <http://www.nasdr.com/pdf-text/0377ntm.pdf>. The substance of the proposed new requirements would appear in Rule 2210. Rule 2211 would be amended to subject institutional sales material and correspondence to Rule 2210's new requirements. 2 (2) The maximum sales charge imposed on purchases or the maximum contingent deferred sales charge computed in accordance with Item 3 of Form N-1A; and (3) Annual fund operating expenses, computed as a percentage of total net assets in accordance with Item 3 of Form N-1A, as of the most recent calendar quarter. The amended rule would additionally require that this disclosure be set forth in "a prominent text box" that only includes this required information and that it appear in a type size "at least as large as that used to present any non-standardized performance."² According to the Notice, while the NASD recognizes that standardized mutual fund performance information already reflects the fund's sales load

and expenses, the proposed revisions “would provide investors with critical information about the annual expenses that they would incur.” Also, the amendments would ensure that standardized performance information is presented “with sufficient prominence and clarity.” Included as Attachment B to the Notice is “Sample Disclosure,” which is not discussed in the Notice but which, presumably, is a sample of disclosure that would comply with the proposed revisions. This sample reads as follows: [performance numbers.] These performance numbers reflect the deduction of the fund’s maximum [front-end/back-end] sales charge and annual expenses. The fund’s current maximum [front-end/back-end] sales charge is __% and the fund’s current annual expenses are __% of the fund’s net assets. In addition to seeking comment on the proposed rule revisions, the Notice seek comment on the following: • Should other types of information also be required to be disclosed – e.g., instead of disclosure of a fund’s expense ratio, should disclosure be required of the actual dollar amount of expenses incurred by a hypothetical shareholder in the fund? Should the proposed requirements apply to investment company sales material that does not present performance information – e.g., should funds that hold themselves out as “no- load” have to disclose the fund’s annual expense ratio in all sales material? Dorothy M. Donohue Associate Counsel 2 For communications delivered through electronic media, these requirements may be satisfied by presenting the information in a manner that is intended to draw investor attention to it. For radio, television, and video advertisements, the required information must be given emphasis equal to that given to any non-standardized performance information.