

MEMO# 11430

November 29, 1999

SEC APPROVAL OF AMENDMENTS TO NASD SALES CHARGE RULE

* SEC Release No. 34-42043 (October 20, 1999), 64 Fed. Reg. 58112 (October 28, 1999). [11430] November 29, 1999 TO: OPERATIONS COMMITTEE No. 45-99 TRANSFER AGENT ADVISORY COMMITTEE No. 74-99 RE: SEC APPROVAL OF AMENDMENTS TO NASD SALES CHARGE RULE

The Securities and Exchange Commission has approved amendments to NASD Conduct Rule 2830 concerning mutual fund sales charges. The rule amendments revise Rule 2830 to: (1) impose maximum aggregate sales charge limits on funds of funds; (2) permit mutual funds to charge installment loads; (3) prohibit loads on reinvested dividends; (4) impose redemption order requirements for shares subject to contingent deferred sales charges; and (5) eliminate duplicative prospectus disclosure. A copy of the SEC's adopting release* is attached and it is summarized below. We understand that NASD Regulation, Inc. ("NASDR") plans to issue a Notice to Members in the near future discussing the amendments and setting forth the amended rule text.

Sales Charge Limits for Funds of Funds The amendments address fund of fund structures in which distribution fees are charged at both the acquiring and underlying fund levels. In particular, under the amended rules, asset-based sales charges imposed by the acquiring and underlying funds in the aggregate may not exceed .75% of average net assets. Similarly, any service fee charged by the acquiring fund and the underlying fund may not, in the aggregate, exceed .25% of average net assets. Although the aggregate asset-based sales charges of funds of funds are not subject to the cumulative sales charge limits in Rule 2830 that apply to other funds with asset-based sales charges, the acquiring and underlying funds remain individually subject to those limits. In response to a comment made by the Institute about the unduly broad scope of the proposed definition of "fund of funds," NASDR has modified the definition to cover only those investment companies that acquire securities of other investment companies in excess of the limits set forth in Section 12(d)(1)(A) of the Investment Company Act of 1940.

Deferred Sales Charges The amendments conform the definition of "deferred sales charge" in Rule 2830 to the definition in Rule 6c-10 under the Investment Company Act. As a result, a fund with an installment load will be subject to the NASD sales charge limits (as required by Rule 6c-10) and to the prohibition on describing a fund as "no load" if it has a deferred sales charge.

Loads on Reinvested Dividends The amendments prohibit the imposition of front-end or deferred sales charges on reinvested dividends. The Institute and several representatives of UIT sponsors opposed this change. The adopting release expresses NASDR's view that loads on reinvested dividends constitute excessive sales charges, regardless of the type of investment company that imposes them. It also describes NASDR's responses to some of the specific arguments raised by commenters. Although the adopting release indicates that a proposed "grandfather clause" for existing

UITs has been eliminated from the final amendments, we have been informed by NASDR staff that this statement is in error. According to NASDR staff, the prohibition on sales charges on reinvested dividends will not apply to investment companies whose registration statements become effective before April 1, 2000. CDSL Calculations The amendments reinstate a requirement previously applicable under Rule 6c-10 concerning the order in which fund shares subject to a contingent deferred sales load must be redeemed when an investor redeems some, but not all, of his or her fund shares. Under the amendments, a first-in/first-out redemption order requirement will apply to partial redemptions, unless another redemption order would result in a redeeming shareholder paying a lower CDSL (in which case the other method may be used). Prospectus Disclosure The amendments eliminate a former requirement that a fund with an asset-based sales charge disclose in its prospectus that long-term shareholders may pay more than the economic equivalent of the maximum front-end sales charges permitted by Rule 2830. This disclosure became duplicative and unnecessary as a result of the SEC's March 1998 amendments to Form N-1A, which require similar prospectus disclosure. Frances M. Stadler Deputy Senior Counsel Attachment

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