

July 19, 1998

Katherine A. England
Assistant Director
Division of Market Regulation
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549
Mail Stop 10-1

Re: **SR-NASD-98-14, Amendment No. 5**
Proposed Rule Change Relating to Sales Charges for Mutual Funds and
Variable Contracts

Dear Ms. England:

Pursuant to Rule 19b-4, NASD Regulation, Inc. is submitting Amendment No. 5 to the above referenced rule filing. This amendment addresses the public comments received by the Securities and Exchange Commission in response to the publication in the Federal Register of the Notice of Filing of Proposed Rule Change Relating to Sales Charges for Investment Companies and Variable Contracts, SR-NASD-98-14.* Our letter to you dated June 3, 1999, which discusses our responses to the comments to the proposed rule change, and which includes the amended proposed rule change language, is enclosed and incorporated by reference. At your request, we also have enclosed a chronology regarding the various filings related to this proposed rule change that preceded this filing.

You have also requested that we respond more specifically to the comments of Battle Fowler LLP and Chapman and Cutler. These commenters have argued that the proposed prohibition of sales charges on shares purchased through reinvested dividends would require unit investment trusts (UITs) that offer deferred sales load structures to create multiple classes of shares. We have discussed this issue with the staff of the Division of Investment Management. Based on our discussions with the staff, we concur with their conclusion that the proposed prohibition would not result in the creation of a senior security for purposes of Section 18 of the Investment Company Act of 1940, and thus would not require UITs to create a multiple class structure.

* 63 Fed. Reg. 43974 (Aug. 17, 1998).

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If you have any questions, please contact Joseph P. Savage, Counsel, Advertising/Investment Companies Regulation, NASD Regulation, Inc., (telephone: (202) 728-8233; e-mail: savagejp@nasd.com) or me (telephone: (202) 728-8068; e-mail: selmant@nasd.com). The fax number is (202) 974-2732.

Very truly yours,

Thomas M. Selman
Vice President

Attachments

cc: Christine M. Richardson
SEC Division of Market Regulation

Alison M. Fuller
SEC Division of Investment Management

Sales Charge Rule Amendments Chronology

July 19, 1999

At the request of the Division of Market Regulation, the NASD Regulation staff has prepared this chart, which sets forth dates and descriptions of the series of filings that NASD Regulation has made with the SEC in connection with its efforts to amend its Conduct Rules 2820 and 2830, governing the sales charges for investment companies and variable contracts.

The National Securities Markets Improvement Act of 1996 (NSMIA) permitted the creation of so-called “funds of funds,” provided that the sales charges imposed by such funds are not excessive under NASD or SEC rules. NASD Regulation had intended that the proposed amendments accommodate this statutory mandate. Today Rule 2830 does not contemplate sales charges imposed by funds of funds.

This chronology also includes the date on which the SEC approved other amendments to Rules 2820 and 2830 relating to non-cash compensation arrangements. This date is included to clarify the timing of the non-cash amendments, relative to the publication of proposed sales charge amendments.

<u>Date</u>	<u>Event</u>	<u>Description</u>
Feb. 17, 1998	Initial Filing	<p>In response to NSMIA and other developments, NASD Regulation initially submits the proposed changes to the SEC staff.</p> <p>The staff subsequently directs NASD Regulation to submit an amendment that adds a sentence stating that NASD Regulation believes that the proposed changes are consistent with Section 15A(b)(6) of the 1934 Act.</p>
Mar. 12, 1998	Amendment No. 1	<p>NASD Regulation submits an amended filing with the requested language.</p> <p>The SEC staff subsequently provides comments on the rule proposal.</p>

June 11, 1998	Amendment No. 2	NASD Regulation submits an amendment that responds to the SEC staff comments. SEC staff, rather than reviewing the filing as to its substance, subsequently rejects it on the ground that it was insufficient as to form. The SEC staff specifically objects to the fact that the rule changes from the original proposal were italicized, to make it easier for the SEC staff to analyze.
July 13, 1998	Amendment No. 3	NASD Regulation once again files a revised proposed rule change, without the italics.
July 15, 1998	SEC Approves Non-Cash Compensation Amendments	SEC approves amendments to NASD Conduct Rules 2820 and 2830 relating to the regulation of non-cash compensation arrangements for the sale and distribution of variable contracts and investment company securities.
After July 15, 1999	SEC Requests for Technical Changes	The SEC staff requests certain grammatical and technical changes to Amendment No. 3 to the Sales Charge Rule filed on July 13.
Aug. 12, 1998	Amendment No. 4	NASD Regulation files another revised proposed rule change in response to SEC staff's non-substantive comments on Amendment No. 3. This filing does not reflect the unrelated non-cash amendments to Rule 2830.
Aug. 17, 1998	Federal Register Publication of Proposal	SEC staff publishes for comment in the Federal Register the proposed changes to NASD Conduct Rules 2820 and 2830. <i>See</i> 63 Fed. Reg. 43974 (Aug. 17, 1998). Proposed changes do not include or refer to rules changes regarding non-cash compensation arrangements.
Sept. 8, 1998	Comment Period Expires	Comment period on sales charge rule proposal expires.

Dec. 17, 1998	Extension No. 1	NASD Regulation submits a letter extending the time for SEC action on the rule proposal to January 30, 1999. Extension requested due to staffing changes in Advertising/Investment Companies Regulation Department.
June 3, 1999	Response to Comments	<p>NASD Regulation files with SEC a letter responding to the comments submitted in response to the SEC's August 1998 publication of the proposed changes to NASD Conduct Rules 2820 and 2830.</p> <p>SEC staff subsequently objects to filing on ground that its "re" line is incorrect.</p> <p>Staff subsequently requests this chronology.</p> <p>Staff subsequently requests clarification of multi-class issue.</p>
July 19, 1999	Amendment No. 5	NASD Regulation files a letter with corrected "re" line, chronology and explanation of multi-class issue; deems filing to be Amendment No. 5.

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June 3 1999

Katherine A. England
Assistant Director
Division of Market Regulation
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549

Re: File No. SR-NASD-98-14 – Proposed Rule Change by the National Association
of Securities Dealers, Inc. Concerning Sales Charge Limitations

Dear Ms. England:

This letter summarizes and responds to comment letters submitted in response to the Securities and Exchange Commission's ("SEC") publication of proposed changes to National Association of Securities Dealers, Inc. ("NASD") Conduct Rules 2820 and 2830.² Commenters consist of Battle Fowler LLP ("Battle Fowler"), Cahill Gordon & Reindel ("Cahill Gordon"), Carter, Ledyard & Milburn ("Carter Ledyard"), Chapman and Cutler, Davis Polk & Wardell ("Davis Polk"), the Investment Company Institute ("ICI"), the National Association for Variable Annuities ("NAVA"), and Prudential Securities Incorporated ("Prudential").

1. *Prohibition of Sales Loads on Reinvested Dividends*

Battle Fowler, Carter Ledyard, Chapman and Cutler, Davis Polk, the ICI and Prudential opposed the proposed prohibition of loads on shares purchased through reinvestment of dividends, as that prohibition would apply to sponsors of unit investment trusts ("UITs"). Some commenters asserted that this prohibition is not justified, since a UIT investor does not pay a sales charge twice on the same assets when he or she purchases shares through reinvested dividends. Moreover, some commenters pointed out that unlike mutual funds underwriters, UIT

² See Securities and Exchange Commission Release No. 34-40310 (Aug. 7, 1998), 63 Fed. Reg. 43974 (Aug. 17, 1998).

sponsors are not permitted to receive fees pursuant to Rule 12b-1 under the Investment Company Act of 1940 (the "1940 Act"), since UITs do not have boards of directors (whose approval is required for Rule 12b-1 plans). Thus, these commenters urged that UIT sponsors should be permitted to recoup their expenses through sales charges imposed on reinvested dividends.

Several commenters asserted that prohibiting such sales charges would be inconsistent with SEC exemptive orders that permit certain UIT sponsors to impose sales charges on reinvested dividends, subject to certain conditions. Battle Fowler and Chapman and Cutler asserted that this prohibition would require certain UITs that offer deferred sales load structures to create multiple classes of shares, which could raise issues under the 1940 Act and the federal tax laws.

Carter Ledyard and Davis Polk argued that the proposed prohibition would require UIT sponsors to reprogram their computer systems to separate reinvestment shares when deferred sales loads are deducted. The SEC has issued a moratorium on the implementation of new SEC rules that require major reprogramming of SEC-regulated entities' computer systems between June 1, 1999 and March 31, 2000, in order to allow these entities to focus their efforts on resolving any Year 2000 computer programming issues.³ These commenters questioned the SEC's authority to approve this aspect of the proposed rule change in light of its Y2K moratorium.

Response: NASD Regulation continues to believe that loads on reinvested dividends constitute excessive compensation, regardless of the type of investment company that imposes them. We are not persuaded by the arguments that the proposed amendments conflict with certain SEC exemptive orders.

Some comment letters indicated that exemptive relief under the 1940 Act was necessary in order for UIT sponsors to charge installment loads on reinvested dividends, and that the SEC had granted this relief. We have reviewed the exemptive orders and related notices cited by the comment letters. While these orders permitted UIT sponsors to charge installment loads, they do not appear to refer to any dividend reinvestment program. Indeed, we understand that at least two of these orders applied to fixed portfolio UITs that offered only dividend reinvestment into no-load mutual funds.⁴ Moreover, the exemptive orders provide relief from the application of certain provisions of the 1940 Act and the SEC rules thereunder. The orders do not address or provide relief from the application of the NASD's Conduct Rules.

³ Securities and Exchange Commission Release No. 34-40377 (Aug. 27, 1998), 63 Fed. Reg. 47051 (Sept. 3, 1998).

⁴ Compare, e.g., Letter to Jonathan G. Katz, Securities and Exchange Commission from Davis Polk (September 8, 1998) (citing Release Nos. IC-15167 and IC -13848) with Letter to R. Clark Hooper, NASD, Inc. from Davis Polk (October 14, 1993) (seeking interpretation that UITs subject to these orders qualify for higher sales charge caps in part because they offer reinvestment into no-load mutual funds).

We also discussed with the SEC staff the issue of whether UITs would have to create multiple classes of shares to comply with the proposed prohibition on loads on reinvested dividends and one commenter's claim that a multiple class structure could cause adverse tax consequences for UITs. We defer to the expertise of the Division of Investment Management on this issue. In our view, however, complying with the proposed amendments should not require UITs to adopt a multiple class structure.

We also do not agree with the offered comparisons to Rule 12b-1 fees. Our determination that loads on reinvested dividends are excessive was unrelated to the question of whether Rule 12b-1 fees may be charged. Thus, for example, the prohibition would apply to mutual funds that have no Rule 12b-1 plan just as it applies to mutual funds that have Rule 12b-1 plans. As amended, Rule 2830(d)(6)(B) would not prohibit UIT sponsors from imposing sales charges on the initial purchase of UIT shares, which UIT sponsors may set at a level that should adequately compensate them for their distribution costs.

Nevertheless, NASD Regulation does recognize that prohibiting sales loads on reinvested dividends could require UIT sponsors to reprogram their computer systems. We further recognize that the SEC's moratorium on the implementation of new rules that require major reprogramming of computer systems may preclude approval of this rule if it were to take effect prior to April 1, 2000. Accordingly, NASD Regulation proposes to revise Rule 2830(d)(6)(B) to delay the effectiveness of the prohibition of loads on reinvested dividends with respect to UITs until April 1, 2000, in order to comply with the Y2K moratorium.

2. *"Fund of Funds" Definition*

Chapman and Cutler and the ICI both recommended changes to the proposed definition of "fund of funds" in Rule 2830(b)(11). The proposed amendments published by the SEC would have defined "fund of funds" as "an investment company that invests any portion of its assets in the securities of registered open-end investment companies or registered unit investment trusts." Both commenters felt that this language was too broad and may unnecessarily include funds that invest only a small portion of their assets in other funds. The commenters noted that Section 12(d)(1)(A) of the 1940 Act permits an investment company to purchase a limited amount of the total voting stock of another investment company.⁵ Chapman and Cutler and the ICI suggested that the definition of "fund of funds" be modified to more closely reflect traditional funds of funds, such as those companies relying on Sections 12(d)(1)(F) and 12(d)(1)(G) of the 1940 Act. Alternatively, the ICI recommended that the definition include only funds whose investments in other funds exceed the limits permitted under Section 12(d)(1)(A).

⁵ In particular, Section 12(d)(1)(A) permits an investment company to invest in up to 3% of the shares of another fund, provided that the value of such shares represents less than 5% of the acquiring fund's total assets, and the acquiring fund's investments in all other funds represent less than 10% of the acquiring fund's total assets.

Response: NASD Regulation proposes to modify the definition of “fund of funds” to include any investment company that acquires securities issued by any other investment company in excess of the amounts permitted under Section 12(d)(1)(A) of the 1940 Act. This definition will exclude from the definition investment companies that invest only a small portion of their assets in other funds’ shares.

3. Calculation of Contingent Deferred Sales Loads

The proposed amendments would reinstate requirements previously applicable pursuant to SEC Rule 6c-10 under the 1940 Act concerning the order in which fund shares subject to a contingent deferred sales load (“CDSL”) must be redeemed. (See Rule 2830(d)(6)(A).) If a fund has a CDSL that declines over the shareholder’s investment period, then the proposed amendments would require the fund to calculate the CDSL as if the shares not subject to the CDSL are redeemed first, and other shares are then redeemed in the order purchased, provided that another order or redemption may be used if it results in the shareholder paying a lower CDSL. Chapman and Cutler commented that some investors for business or tax reasons may want to apply a different order of redemption than the one specified by the rule, and that therefore the rule should be modified to allow investors to dictate a different order of redemption. The ICI commented that, while it does not object to this provision, it believes that it should be modified to specify that it applies to partial redemptions. The ICI also recommended that the rule language be modified to provide that an order of redemption other than first-in-first-out may be used if such an order “could” (rather than “would”) result in the shareholder paying a lower CDSL.

Response: NASD Regulation does not believe additional changes are needed to this provision. NASD Regulation is not aware of any significant problems that arose as a result of the identical requirements that were previously imposed on the investment company industry by Rule 6c-10. Moreover, we are concerned that if investors were permitted to consent to a different order of redemption, investment company account agreements could include standard language that effectively allows a fund sponsor to determine the order of redemption. We also do not believe that it is necessary to modify the language of this provision to indicate that it applies only to partial redemptions, since if all shares are redeemed, the issue of redemption order becomes moot.

4. Elimination of Variable Annuity Sales Charge Restrictions

NAVA commented that it strongly supports elimination of the limits in Rule 2820 on variable annuity sales loads. NAVA noted that the National Securities Markets Improvement Act of 1996 (“NSMIA”) amended Section 26 of the 1940 Act to exempt variable annuities from the charge restrictions in Sections 26 and 27 of the 1940 Act. NSMIA substituted in their place a requirement that variable contract charges be reasonable in relation to the services rendered. NAVA commented that the imposition of sales charge restrictions on variable annuities would be inconsistent with the purpose and intent of this amendment. NAVA also expressed its support

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for NASD Regulation's decision not to impose sales charge limits in Rule 2830 on funds underlying variable annuities, again citing the NSMIA amendments to Section 26 of the 1940 Act.

Response: The proposed amendments as revised, like the original proposal, would eliminate the restrictions on variable annuity sales loads and would not impose sales charge limits on funds underlying variable annuities.

Very truly yours,

Thomas M. Selman

Attachment

cc: Kenneth Berman
Division of Investment Management
Securities and Exchange Commission

Christine M. Richardson
Division of Market Regulation
Securities and Exchange Commission

ATTACHMENT

TEXT OF PROPOSED AMENDMENTS

(**Note:** New text is italicized; deletions are bracketed. Rule 2820 paragraphs (a)-(b) and Rule 2830 paragraphs (e)-(n) are not included; no amendments to those paragraphs are proposed.)

I. 2820 VARIABLE CONTRACTS OF AN INSURANCE COMPANY

(a) - (b) No change

[(c) Sales Charges]

[No member shall participate in the offering or in the sale of variable annuity contracts if the purchase payment includes a sales charge which is excessive:]

[(1) Under contracts providing for multiple payments a sales charge shall not be deemed to be excessive if the sales charge stated in the prospectus does not exceed 8.5% of the total payments to be made thereon as of a date not later than the end of the twelfth year of such payments, provided that if a contract be issued for any stipulated shorter payment period, the sales charge under such contract shall not exceed 8.5% of the total payments thereunder for such period.]

[(2) Under contracts providing for single payments a sales charge shall not be deemed to be excessive if the prospectus sets forth a scale of reducing sales charges related to the amount of the purchase payment which is not greater than the following schedule:

First \$25,000 - 8.5% of purchase payment
Next \$25,000 - 7.5% of purchase payment
Over \$50,000 - 6.5% of purchase payment]

[(3) Under contracts where sales charges and other deductions for purchase payments are not stated separately in the prospectus the total deductions from purchase payments (excluding those for insurance premiums and premium taxes) shall be treated as a sales charge for purposes of this rule and shall not be deemed to be excessive if they do not exceed the percentages for multiple and single payment contracts described in paragraphs (1) and (2) above.]

[(4) Every member who is an underwriter and/or issuer of variable annuities shall file with Advertising/Investment Companies Regulation

Department, prior to implementation, the details of any changes or proposed changes in the sales charges of such variable annuities, if the changes or proposed changes would increase the effective sales charge on any transaction. Such filings should be clearly identified as an "Amendment to Variable Annuity Sales Charges."]

[(d)] (c) Receipt of Payment

No member shall participate in the offering or in the sale of a variable contract on any basis other than at a value to be determined following receipt of payment therefor in accordance with the provisions of the contract, and, if applicable, the prospectus, the Investment Company Act of 1940 and applicable rules thereunder. Payments need not be considered as received until the contract application has been accepted by the insurance company, except that by mutual agreement [it] *they* may be considered to have been received for the risk of the purchaser when actually received.

[(e)] (d) Transmittal

Every member who receives applications and/or purchase payments for variable contracts shall transmit promptly to the issuer all such applications and at least that portion of the purchase payment required to be credited to the contract.

[(f)] (e) Selling Agreement

No member who is a principal underwriter as defined in the Investment Company Act of 1940 may sell variable contracts through another broker/dealer unless (1) such broker/dealer is a member, and (2) there is a sales agreement in effect between the parties. Such sales agreement must provide that the sales commission be returned to the issuing insurance company if the variable contract is tendered for redemption within seven business days after acceptance of the contract application.

[(g)] (f) Redemption

No member shall participate in the offering or in the sale of a variable contract unless the insurance company, upon receipt of a request in proper form for partial or total redemption in accordance with the provisions of the contract undertakes to make prompt payment of the amounts requested and payable under the contract in accordance with the terms thereof, and, if applicable, the prospectus, the Investment Company Act of 1940 and applicable rule thereunder.

[(h)] (g) Member Compensation

In connection with the sale and distribution of variable contracts:

(1) Except as described below, no associated person of a member shall accept any compensation from anyone other than the member with which the person is associated. This requirement will not prohibit arrangements where a non-member company pays compensation directly to associated persons of the member, provided that:

(A) the arrangement is agreed to by the member;

(B) the member relies on an appropriate rule, regulation, interpretive release, interpretive letter, or "no-action" letter issued by the Securities and Exchange Commission that applies to the specific fact situation of the arrangement;

(C) the receipt by associated persons of such compensation is treated as compensation received by the member for purposes of NASD rules; and

(D) the recordkeeping requirement in subparagraph (h)(3) is satisfied.

(2) No member or person associated with a member shall accept any compensation from an offeror which is in the form of securities of any kind.

(3) Except for items as described in subparagraphs (h)(4)(A) and (B), a member shall maintain records of all compensation received by the member or its associated persons from offerors. The records shall include the names of the offerors, the names of the associated persons, the amount of cash, the nature and, if known, the value of non-cash compensation received.

(4) No member or person associated with a member shall directly or indirectly accept or make payments or offers of payments of any non-cash compensation, except as provided in this provision. Notwithstanding the provisions of subparagraph (h)(1), the following non-cash compensation arrangements are permitted:

(A) Gifts that do not exceed an annual amount per person fixed periodically by the Board of Governors⁶ and are not preconditioned on achievement of a sales target.

(B) An occasional meal, a ticket to a sporting event or the theater, or comparable entertainment which is neither so frequent nor so extensive as to raise any question of propriety and is not preconditioned on achievement of a sales target.

(C) Payment or reimbursement by offerors in connection with meetings held by an offeror or by a member for the purpose of training or education of associated persons of a member, provided that:

(i) the recordkeeping requirement in subparagraph (h)(3) is satisfied;

(ii) associated persons obtain the member's prior approval to attend the meeting and attendance by a member's associated persons is not preconditioned by the member on the achievement of a sales target or any other incentives pursuant to a non-cash compensation arrangement permitted by subparagraph (h)(4)(D);

(iii) the location is appropriate to the purpose of the meeting, which shall mean an office of the offeror or the member, or a facility located in the vicinity of such office, or a regional location with respect to regional meetings;

(iv) the payment or reimbursement is not applied to the expenses of guests of the associated person; and

(v) the payment or reimbursement by the offeror is not preconditioned by the offeror on the achievement of a sales target or any other non-cash compensation arrangement permitted by subparagraph (h)(4)(D).

(D) Non-cash compensation arrangements between a member and its associated persons or a non-member company and its sales personnel who are associated persons of an affiliated member, provided that:

⁶ The current annual amount fixed by the Board of Governors is \$100.

(i) the member's or non-member's non-cash compensation arrangement, if it includes variable contracts, is based on the total production of associated persons with respect to all variable contracts distributed by the member;

(ii) the non-cash compensation arrangement requires that the credit received for each variable contract is equally weighted;

(iii) no unaffiliated non-member company or other unaffiliated member directly or indirectly participates in the member's or non-member's organization of a permissible non-cash compensation arrangement; and

(iv) the recordkeeping requirement in subparagraph (h)(3) is satisfied.

(E) Contributions by a non-member company or other member to a non-cash compensation arrangement between a member and its associated persons, or contributions by a member to a non-cash compensation arrangement of a non-member, provided that the arrangement meets the criteria in subparagraph (h)(4)(D).

II. 2830 INVESTMENT COMPANY SECURITIES

(a) Application

This Rule shall apply exclusively to the activities of members in connection with the securities of companies registered under the Investment Company Act of 1940 (*“the 1940 Act”*); provided, however, that Rule 2820 shall apply, in lieu of this Rule, to members’ activities in connection with “variable contracts” as defined therein.

(b) Definitions

(1) The terms “affiliated member,” “compensation,” “cash compensation,” “non-cash compensation” and “offeror” as used in paragraph (1) of this section shall have the following meanings:

"Affiliated Member" shall mean a member which, directly or indirectly, controls, is controlled by, or is under common control with a non-member company.

“Compensation” shall mean cash compensation and non-cash compensation.

“Cash compensation” shall mean any discount, concession, fee, service fee, commission, asset-based sales charge, loan, override or cash employee benefit received in connection with the sale and distribution of investment company securities.

“Non-cash compensation” shall mean any form of compensation received in connection with the sale and distribution of investment company securities that is not cash compensation, including but not limited to merchandise, gifts and prizes, travel expenses, meals and lodging.

“Offeror” shall mean an investment company, an adviser to an investment company, a fund administrator, an underwriter and any affiliated person (as defined in Section 2(a)(3) of the [Investment Company Act of 1940] *1940 Act*) of such entities.

(2) “Brokerage commissions,” as used in paragraph (k), shall not be limited to commissions on agency transactions but shall include underwriting discounts or concessions and fees to members in connection with tender offers.

(3) “Covered account,” as used in paragraph (k), shall mean (A) any other investment company or other account managed by the investment adviser of such investment company, or (B) any other account from which brokerage commissions are received or expected as a result of the request or direction of any principal underwriter of such investment company or of any affiliated person (as defined in the [Investment Company Act of 1940] *1940 Act*) of such investment company or of such underwriter, or of any affiliated person of an affiliated person of such investment company.

(4) “Person” shall mean “person” as defined in the [Investment Company Act of 1940] *1940 Act*.

(5) “Prime rate,” as used in paragraph (d), shall mean the most preferential interest rate on corporate loans at large U.S. money center commercial banks.

(6) “Public offering price” shall mean a public offering price as set forth in the prospectus of the issuing company.

(7) “Rights of accumulation,” as used in paragraph (d), shall mean a scale of reducing sales charges in which the sales charge applicable to the securities

being purchased is based upon the aggregate quantity of securities previously purchased or acquired and then owned plus the securities being purchased.

The quantity of securities owned shall be based upon:

(A) The current value of such securities (measured by either net asset value or maximum offering price); or

(B) Total purchases of such securities at actual offering prices; or

(C) The higher of the current value or the total purchases of such securities.

The quantity of securities owned may also include redeemable securities of other registered investment companies having the same principal underwriter.

(8) “Sales Charge” and “sales charges,” as used in paragraph (d), shall mean all charges or fees that are paid to finance sales or sales promotion expenses, including front-end deferred and asset-based sales charges, excluding charges and fees for ministerial, recordkeeping or administrative activities and investment management fees. For purposes of this Rule, members may rely on the sales-related fees and charges disclosed in the prospectus of an investment company.

(A) An “asset-based sales charge” is a sales charge that is deducted from the net assets of an investment company and does not include a service fee.

(B) A “deferred sales charge” is [a sales charge that is deducted from the proceeds of the redemption of shares by an investor, excluding any such charges that are (i) nominal and are for services in connection with a redemption or (ii) discourage short-term trading, that are not used to finance sales-related expenses, and that are credited to the net assets of the investment company] *any amount properly chargeable to sales or promotional expenses that is paid by a shareholder after purchase but before or upon redemption.*

(C) A “front-end sales charge” is a sales charge that is included in the public offering price of the shares of an investment company.

(9) “Service fees,” as used in paragraph (d), shall mean payments by an investment company for personal service and/or the maintenance of shareholder accounts.

(10) The terms “underwriter,” “principal underwriter,” “redeemable security,” “periodic payment plan,” “open-end management investment company,” and “unit investment trust,” shall have the same definitions used in the [Investment Company Act of 1940] *1940 Act*.

(11) A “*fund of funds*” is an investment company that acquires securities issued by any other investment company in excess of the amounts permitted under paragraph (A) of Section 12(d)(1) of the 1940 Act. An “*acquiring company*” in a fund of funds is the investment company that purchases or otherwise acquires the securities of another investment company, and an “*acquired company*” is the investment company whose securities are acquired.

(12) “*Investment companies in a single complex*” are any two or more companies that hold themselves out to investors as related companies for purposes of investment and investor services.

(c) Conditions of Discounts to Dealers

No member who is an underwriter of the securities of an investment company shall sell any such security to any dealer or broker at any price other than a public offering price unless such sale is in conformance with Rule 2420 and, if the security is issued by an open-end management company or by a unit investment trust which invests primarily in securities issued by other investment companies, unless a sales agreement shall set forth the concessions to be received by the dealer or broker.

(d) Sales Charge

No member shall offer or sell the shares of any open-end investment company or any “single payment” investment plan issued by a unit investment trust (collectively “investment companies”) registered under the [Investment Company Act of 1940] *1940 Act* if the sales charges described in the prospectus are excessive. Aggregate sales charges shall be deemed excessive if they do not conform to the following provisions:

(1) Investment Companies Without an Asset-Based Sales Charge

(A) *Aggregate* front-end and[/or] deferred sales charges described in the prospectus which may be imposed by an investment company without an asset-based sales charge shall not exceed 8.5% of the offering price.

[(B) (i) Dividend reinvestment may be made available at net asset value per share to any person who requests such reinvestment.

(ii) If dividend reinvestment is not made available as specified in subparagraph (B)(i) above, the maximum aggregate sales charge shall not exceed 7.25% of offering price.]

[(C)](B)(i) Rights of accumulation (cumulative quantity discounts) may be made available to any person in accordance with one of the alternative quantity discount schedules provided in subparagraph [(D)](C)(i) below, as in effect on the date the right is exercised.

(ii) If rights of accumulation are not made available on terms at least as favorable as those specified in subparagraph (C)(i) the maximum aggregate sales charge shall not exceed[:]

[a)] 8.0% of offering price. [if the provisions of subparagraph (B)(i) are met; or

(b) 6.75% of offering price if the provisions of subparagraph (B)(i) are not met.]

[(D)](C)(i) Quantity discounts, if offered, shall be made available on single purchases by any person in accordance with one of the following two alternatives:

a. A maximum aggregate sales charge of 7.75% on purchases of \$10,000 or more and a maximum aggregate sales charge of 6.25% on purchases of \$25,000 or more, or

b. A maximum aggregate sales charge of 7.50% on purchases of \$15,000 or more and a maximum aggregate sales charge of 6.25% on purchases of \$25,000 or more.

(ii) If quantity discounts are not made available on terms at least as favorable as those specified in subparagraph [(D)](C)(i) the maximum aggregate sales charge shall not exceed:

a. 7.75% of offering price if the provisions of subparagraph[s (B)(i) and (C)(i)] (B) are met.

b. 7.25% of offering price if [the provisions of subparagraph (B)(i) are met but] the provisions of subparagraph [(C)(i)](B) are not met.

[c. 6.50% of offering price if the provisions of subparagraph (C) (i) are met but the provision of subparagraph (B)(i) are not met.]

[d. 6.25% of offering price if the provisions of subparagraphs (B)(i) and (C)(i) are not met.]

[(E)] (D) If an investment company without an asset-based sales charge pays a service fee, the maximum aggregate sales charge shall not exceed 7.25% of the offering price.

[(F) If an investment company without an asset-based sales charge reinvests dividends at offering price, it shall not offer or pay a service fee unless it offers quantity discounts and rights of accumulation and the maximum aggregate sales charge does not exceed 6.25% of the offering price.]

(2) Investment Companies With an Asset-Based Sales Charge

(A) Except as provided in subparagraphs (C) and (D), the aggregate asset-based, front-end and deferred sales charges described in the prospectus which may be imposed by an investment company with an asset-based sales charge, if the investment company has adopted a plan under which service fees are paid, shall not exceed 6.25% of total new gross sales (excluding sales from the reinvestment of distributions; [and] exchanges of shares between investment companies in a single complex, between classes [of shares] of an investment company with multiple classes of shares or between series [shares] of a series investment company) plus interest charges on such amount equal to the prime rate plus one percent per annum. The maximum front-end or deferred sales charge resulting from any transaction shall be 6.25% of the amount invested.

(B) Except as provided in subparagraphs (C) and (D), if an investment company with an asset-based sales charge does not pay a service fee, the aggregate asset-based, front-end and deferred sales charges described in the prospectus shall not exceed 7.25% of total new gross sales (excluding sales from the reinvestment of distributions; [and] exchanges of shares between investment companies in a single complex, between classes [of shares] of an investment company with multiple classes of shares or between series [shares] of a series investment company) plus interest charges on such amount equal to the prime rate plus one percent

per annum. The maximum front-end or deferred sales charge resulting from any transaction shall be 7.25% of the amount invested.

(C) The maximum aggregate sales charge on total new gross sales set forth in subparagraphs (A) and (B) may be increased by an amount calculated by applying the appropriate percentages of 6.25% or 7.25% of total new gross sales which occurred after an investment company first adopted an asset-based sales charge until July 7, 1993 plus interest charges on such amount equal to the prime rate plus one percent per annum less any front-end, asset-based or deferred sales charges on such sales or net assets resulting from such sales.

(D) The maximum aggregate sales charges of an investment company in a single complex, a class or share issued by an investment company with multiple classes of shares or a separate series of a series investment company, may be increased to include sales of exchanged shares provided that such increase is deducted from the maximum aggregate sales charges of the investment company, class or series which redeemed the shares for the purpose of such exchanges.

(E) No member shall offer or sell the shares of an investment company with an asset-based sales charge if:

(i) The amount of the asset-based sales charge exceeds .75 of 1% per annum of the average annual net assets of the investment company; or

(ii) Any deferred sales charges deducted from the proceeds of a redemption after the maximum cap, described in subparagraphs (A), (B), (C) and (D) hereof, has been attained are not credited to the investment company.

(3) *Fund of Funds*

(A) *If neither an acquiring company nor an acquired company in a fund of funds structure has an asset-based sales charge, the maximum aggregate front-end and deferred sales charges that may be imposed by the acquiring company, the acquired company and those companies in combination, shall not exceed the rates provided in paragraph (d)(1).*

(B) *Any acquiring company or acquired company in a fund of funds structure that has an asset-based sales charge shall individually comply with the requirements of paragraph (d)(2), provided:*

(i) If the acquiring and acquired companies are in a single complex and the acquired fund has an asset-based sales charge, sales made to the acquiring fund shall be excluded from total gross new sales for purposes of acquired fund's calculations under subparagraphs (d)(2)(A) through (d)(2)(D); and

(ii) If both the acquiring and acquired companies have an asset-based sales charge: (a) the maximum aggregate asset-based sales charge imposed by the acquiring company, the acquired company and those companies in combination, shall not exceed the rate provided in subparagraph (d)(2)(E)(i); and (b) the maximum aggregate front-end or deferred sales charges shall not exceed 7.25% of the amount invested, or 6.25% if either company pays a service fee.

(C) The rates described in subparagraphs (d)(4) and (d)(5) shall apply to the acquiring company, the acquired company and those companies in combination. The limitations of subparagraph (d)(6) shall apply to the acquiring company and the acquired company individually.

[(3)](4) No member or person associated with a member shall, either orally or in writing, describe an investment as being "no load" or as having "no sales charge" if the investment company has a front-end or deferred sales charge or [whose] *its* total charges against net assets to provide for sales related expenses and/or service fees exceed .25 of 1% of average net asset per annum.

[(4) No member or person associated with a member shall offer or sell the securities of an investment company with an asset-based sales charge unless its prospectus discloses that long-term shareholders may pay more than the economic equivalent of the maximum front-end sales charges permitted by this Rule. Such disclosure shall be adjacent to the fee table in the front section of a prospectus. This subparagraph shall not apply to money market mutual funds which have asset-based sales charges equal to or less than .25 of 1% of average net assets per annum.]

(5) No member or person associated with a member shall offer or sell the securities of an investment company if the service fees paid by the investment company, as disclosed in the prospectus, exceed .25 of 1% of its average annual net assets or if a service fee paid by the investment company, as disclosed in the prospectus, to any person who sells its shares exceeds .25 of 1% of the average annual net asset value of such shares.

(6) No member or person associated with a member shall offer or sell the securities of an investment company if:

(A) The investment company has a deferred sales charge paid upon redemption that declines over the period of a shareholder's investment ("contingent deferred sales load"), unless the contingent deferred sales load is calculated as if the shares or amounts representing shares not subject to the load are redeemed first, and other shares or amounts representing shares are then redeemed in the order purchased, provided that another order of redemption may be used if such order would result in the redeeming shareholder paying a lower contingent deferred sales load; or

(B) The investment company has a front-end or deferred sales charge imposed on shares, or amounts representing shares, that are purchased through the reinvestment of dividends; provided, however, that this requirement shall not apply to investment companies that are structured as unit investment trusts until April 1, 2000.

(e) - (l) No change.