

September 9, 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: **File No. SR-NASD-98-69** - Amendment to Interpretive Material Regarding
Mutual Fund Breakpoint Sales

Dear Ms. England:

Pursuant to Rule 19b-4, enclosed herewith is the above-numbered rule filing. Also enclosed is a 3-1/2" disk containing the rule filing in Microsoft Word 7.0 to facilitate production of the Federal Register release.

If you have any questions, please contact Joseph E. Price, Counsel, Advertising/Investment Companies Regulation, NASD Regulation, Inc., at (202) 728-8877, or Robert J. Smith, Office of General Counsel, NASD Regulation, at (202) 728-8176.

Very truly yours,

Joan C. Conley
Secretary

Attachment

File No. SR-NASD-98-69
Consists of 12 Pages

SECURITIES AND EXCHANGE COMMISSION

Washington, D. C.

Form 19b-4

Proposed Rule Change

by

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

Pursuant to Rule 19b-4 under the
Securities Exchange Act of 1934

1. Text of Proposed Rule Change

Pursuant to the provisions of Section 19(b)(1) under the Securities Exchange Act of 1934 ("Act"), NASD Regulation, Inc. ("NASD Regulation") is filing with the Securities and Exchange Commission ("SEC" or "Commission") a proposed rule change to Interpretive Memorandum 2830-1 of the National Association of Securities Dealers, Inc. ("NASD" or "Association") regarding mutual fund breakpoint sales to clarify its application to modern portfolio investment strategies. Below is the text of the proposed rule change. Proposed new language is underlined.

IM-2830-1 "Breakpoint" Sales

The sale of investment company shares in dollar amounts just below the point at which the sales charge is reduced on quantity transactions so as to share in the higher sales charges applicable on sales below the breakpoint is contrary to just and equitable principles of trade.

Investment company underwriters and sponsors, as well as dealers, have a definite responsibility in such matters and failure to discourage and to discontinue such practices shall not be countenanced.

For purposes of determining whether a sale in dollar amounts just below a breakpoint was made in order to share in a higher sales charge, the Association will consider the facts and circumstances, including, for example, whether a member has retained records that demonstrate that the trade was executed in accordance with a bona fide asset allocation program that the member offers to its customers:

- which is designed to meet their diversification needs and investment goals; and
- under which the member discloses to its customers that they may not qualify for breakpoint reductions that are otherwise available.

2. Procedures of the Self-Regulatory Organization

(a) The proposed rule change was approved by the Board of Directors of NASD Regulation at its meeting on June 25, 1998, and the Board of Governors of the NASD determined not to review the proposed rule change at its meeting on June 25, 1998, which authorized the filing of the rule change with the SEC. Section 1(a)(ii) of Article VII of the NASD By-Laws permits the NASD Board of Governors to adopt amendments to NASD Rules without recourse to the membership for approval. The Nasdaq Stock Market has been provided an opportunity to consult with respect to the proposed rule change, pursuant to the Plan of Allocation and Delegation of Functions by the NASD to its Subsidiaries.

The NASD will announce the effective date of the proposed rule change in a Notice to Members to be published no later than 60 days following Commission approval.

Questions regarding this rule filing may be directed to Joseph E. Price, Counsel, Advertising/Investment Companies Regulation, NASD Regulation, Inc., at (202) 728-8877, or Robert J. Smith, Office of General Counsel, NASD Regulation, at (202) 728-8176.

3. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

(a)

In the context of mutual fund sales, a “breakpoint” is that point at which the sales charge is reduced for quantity purchases of fund shares. Although funds are not required under SEC or NASD rules to offer breakpoint discounts, many funds use the reduced fee

schedules as a marketing tool to attract large investors. NASD Rule IM-2830-1 prohibits sales of mutual fund shares in amounts below breakpoints, if such sales are made “so as to share in higher sales charges.” The application of this standard depends on the purpose, or intent, of the member recommending the transaction. Accordingly, whether a breakpoint sales violation has occurred must depend on facts and circumstances that provide evidence of intent.

Recently, NASD Regulation considered the application of IM-2830-1 to modern portfolio investment strategies that utilize many different mutual funds with varying investment objectives. Both the Independent Dealer/Insurance Affiliate Committee and the Investment Companies Committee requested that the staff consider amending IM-2830-1 to specify more precisely those facts and circumstances the staff will consider when examining whether trades made pursuant to bona fide asset allocation programs that miss breakpoints have violated NASD rules.

NASD Regulation believes that under most circumstances, sales under a breakpoint pursuant to a bona fide asset allocation program would not constitute a breakpoint violation. NASD Regulation also believes that many investors generally may benefit from asset allocation investment strategies, and that such strategies ought not to be discouraged. Based on these factors, as well as a review of the NASD’s past positions regarding breakpoint sales, NASD Regulation proposes to amend IM-2830-1 to provide that for purposes of determining whether a sale was made in a dollar amount below a breakpoint in order to share in a higher commission, the NASD will consider, among other things, whether the member has retained records that demonstrate that the trade was executed in accordance with a bona fide asset

allocation program and customers were informed that they may not receive breakpoint reductions that otherwise would be available.

(b) NASD Regulation believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act, which require, among other things, that the Association's rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest, in that the proposed rule change provides explicit guidance to both members the NASD Regulation examination staff regarding the application of the Association's breakpoint selling rules to modern portfolio investment strategies, such as strategies involving bona fide asset allocation programs, that can benefit investors.

4. Self-Regulatory Organization's Statement on Burden on Competition

NASD Regulation does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended.

5. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Written comments were neither solicited nor received.

6. Extension of Time Period for Commission Action

NASD Regulation does not consent at this time to an extension of the time period for Commission action specified in Section 19(b)(2) of the Act.

7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2)

Not applicable.

8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission

Not applicable.

9. Exhibits

1. Completed notice of proposed rule change for publication in the Federal Register.

Pursuant to the requirements of the Securities Exchange Act of 1934, NASD Regulation has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

NASD REGULATION, INC.

BY: _____
Joan C. Conley, Secretary

Date: September 9, 1998

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34- ; File No. SR-NASD-98-69)

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by National Association of Securities Dealers, Inc. Relating to Mutual Fund Breakpoint Sales

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"), 15 U.S.C. 78s(b)(1), notice is hereby given that on , NASD Regulation, Inc. ("NASD Regulation") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by NASD Regulation. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. SELF-REGULATORY ORGANIZATION'S STATEMENT OF THE TERMS OF SUBSTANCE OF THE PROPOSED RULE CHANGE

NASD Regulation is proposing to amend NASD Interpretive Memorandum 2830-1 regarding mutual fund breakpoint sales to clarify its application to modern portfolio investment strategies. Below is the text of the proposed rule change. Proposed new language is italicized.

IM-2830-1 "Breakpoint" Sales

The sale of investment company shares in dollar amounts just below the point at which the sales charge is reduced on quantity transactions so as to share in the higher sales charges applicable on sales below the breakpoint is contrary to just and equitable principles of trade.

Investment company underwriters and sponsors, as well as dealers, have a definite responsibility in such matters and failure to discourage and to discontinue such practices shall not be countenanced.

For purposes of determining whether a sale in dollar amounts just below a breakpoint was made in order to share in a higher sales charge, the Association will consider the facts and circumstances, including, for example, whether a member has retained records that demonstrate that the trade was executed in accordance with a bona fide asset allocation program that the member offers to its customers:

- which is designed to meet their diversification needs and investment goals; and
- under which the member discloses to its customers that they may not qualify for breakpoint reductions that are otherwise available.

II. SELF-REGULATORY ORGANIZATION'S STATEMENT OF THE PURPOSE OF, AND STATUTORY BASIS FOR, THE PROPOSED RULE CHANGE

In its filing with the Commission, NASD Regulation included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. NASD Regulation has prepared summaries, set forth in Sections (A), (B), and (C) below, of the most significant aspects of such statements.

(A) Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

(a)

In the context of mutual fund sales, a “breakpoint” is that point at which the sales charge is reduced for quantity purchases of fund shares. Although funds are not required

under SEC or NASD rules to offer breakpoint discounts, many funds use reduced fee schedules as a marketing tool to attract large investors. NASD Rule IM-2830-1 prohibits sales of mutual fund shares in amounts below breakpoints, if such sales are made “so as to share in higher sales charges.” The application of this standard depends on the purpose, or intent, of the member recommending the transaction. Accordingly, whether a breakpoint sales violation has occurred must depend on facts and circumstances that provide evidence of intent.

Recently, NASD Regulation considered the application of IM-2830-1 to modern portfolio investment strategies that utilize many different mutual funds with varying investment objectives. Both the Independent Dealer/Insurance Affiliate Committee and the Investment Companies Committee requested that the staff consider amending IM-2830-1 to specify more precisely those facts and circumstances the staff will consider when examining whether trades made pursuant to bona fide asset allocation programs that miss breakpoints have violated NASD rules.

NASD Regulation believes that under most circumstances, sales under a breakpoint pursuant to a bona fide asset allocation program would not constitute a breakpoint violation. NASD Regulation also believes that many investors generally may benefit from asset-based investment strategies, and that such strategies ought not to be discouraged. Based on these factors, as well as a review of the NASD’s past positions regarding breakpoint sales, NASD Regulation proposes to amend IM-2830-1 to provide that for purposes of determining whether a sale was made in a dollar amount below a breakpoint in order to share in a higher commission, the NASD will consider, among other things, whether the member has retained

records that demonstrate that the trade was executed in accordance with a bona fide asset allocation program and customers were informed that they may not receive breakpoint reductions that otherwise would be available.

(b) NASD Regulation believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6)¹ of the Act, which require, among other things, that the Association's rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest, in that the proposed rule change provides explicit guidance to both members the NASD Regulation examination staff regarding the application of the Association's breakpoint selling rules to modern portfolio investment strategies, such as strategies involving bona fide asset allocation programs, that can benefit investors.

(B) Self-Regulatory Organization's Statement on Burden on Competition

NASD Regulation does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended.

(C) Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Written comments were neither solicited nor received.

III. DATE OF EFFECTIVENESS OF THE PROPOSED RULE CHANGE AND TIMING FOR COMMISSION ACTION

Within 35 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it

¹ 15 U.S.C. § 78d-3

finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

- A. by order approve such proposed rule change, or
- B. institute proceedings to determine whether the proposed rule change should be disapproved.

IV. SOLICITATION OF COMMENTS

Interested persons are invited to submit written data, views, and arguments concerning the foregoing. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the NASD. All submissions should refer to the file number in the caption above and should be submitted by [insert date 21 days from the date of publication].

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act, that the proposed rule change be, and hereby is, approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority, 17 CFR 200.30-3(a)(12).

Jonathan G. Katz
Secretary