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Elizabeth M. Murphy
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

RE: Release No. 33-9128; File No. S7-15-10 (Mutual Fund Distribution Fees; Confirmations)

Dear Ms. Murphy:

The Cornell Securities Law Clinic (the "Clinic") welcomes the opportunity to comment on the proposed rule change (the "Rule Proposal") to replace Rule 12b-1 under the Investment Company Act. The Clinic is a Cornell Law School curricular offering in which law students provide legal representation to public investors in the largely rural "Southern Tier" region of upstate New York. For more information, please see http://securities.lawschool.cornell.edu.

The Clinic wholeheartedly supports the approach taken by the Securities and Exchange Commission (the "Commission") to protect the best interests of fund investors. However, as detailed below, the Clinic suggests certain modifications or additions that could be made to the Rule Proposal to improve overall disclosure and transparency.

The Commission believes that the current framework for mutual fund sales-charges and distribution fees is no longer adequate in today's market place for mutual funds, and furthermore, the current framework no longer serves the best interests of fund investors. The Rule Proposal completely eliminates rule 12b-1 of the Investment Company Act. The new Rule 12b-2 coupled with amended Rule 6c-10 will provide the new framework. Additionally, the Commission also proposes improvements to disclosure statement requirements. The Proposed Rules, in general, seek to improve investor understanding of fees and sales charges, and at the same time to protect investors from paying a disproportionate amount of these fees and sales charges in certain mutual fund share classes.

With the large number of people investing their money in mutual funds, it is necessary that the disclosure of fees be as transparent as possible. The small individual investor will rarely be aware of the total amount of fees being charged to his mutual fund account, and furthermore,

probably won't even consider the consequences and effects that an ongoing sales charge will have on his mutual fund investment in the long run. (Rule Proposal at 50-51) Additionally, multiple share class mutual funds present an investment decision which most individual investors are insufficiently informed to make. Consequently, further disclosure requirements are needed. These requirements should outline the different investment possibilities and projections within the different mutual fund share classes.

1. The Clinic Supports the Elimination of Rule 12b-1 and the Adoption of Rule 12b-2

A. The Clinic Supports the "Sales and Marketing Fee" and "Distribution Activity" Designations

The Commission asks whether a term, different from "sales and marketing fee," would be more appropriate. (Rule Proposal at 44) The Commission mentions "sales/service fee" as a possible alternative. The Clinic believes that the term "sales and marketing fee" is appropriate.

Although the "sales and marketing fee" can be used for any type of distribution cost, this designation does a better job of alerting investors of what the fee is intended for, than a simple "service fee" designation would. The Commission explains that the fee will likely be used to pay for servicing fees currently permitted under the NASD Sales Charge Rule, Rule 2830(b)(B)(8). (Rule Proposal at 41) However, the Commission does not intend to limit the fee to only the services described in the NASD rule. Using "distribution fee" or "service fee" is very ambiguous and doesn't alert the investor to how the fund intends to use the money they are being charged. The designation "sales and marketing" is a narrower designation and alerts the investor that the fee will be used to help the fund attract new investments. Furthermore, the Clinic believes that the Commission should highlight the most likely distribution costs that will be paid with the "sales and marketing fee." A footnote in the prospectus mentioning the NASD Sales Charge rule and the costs covered under that rule would be sufficient to alert investors as to the likely use of the "sales and marketing fee."

The Commission also asks whether it should define "distribution activity" differently and whether it should provide more guidance regarding specific expenditures that are distribution expenses and others that are not. (Rule Proposal at 46) The Commission defines "distribution activity" as any activity that is "primarily intended to result in the sale of shares issued by the fund, including, but not necessarily limited to, advertising, compensation of underwriters, dealers, and sales personnel, the printing and mailing of prospectuses to other than current shareholders, and the printing and mailing of sales literature." (Rule Proposal at 45-46) The Clinic believes that this definition of "distribution activity" adequately alerts investors to how investment funds will be using the money they are charging investors. An alternative could be to include every single activity for which the fee is intended, but we believe that this would be an excessive requirement for mutual funds to comply with.

B. The Clinic Supports the 25 Basis Point Cap on the "Sales and Marketing Fee"

The Commission asks whether the limit on the "sales and marketing fee" should be 25 basis points, or whether it should be higher or lower than this amount. (Rule Proposal 44-45) The Clinic believes that the 25 basis points is an adequate cap on the fee. First, 25 basis points is the maximum service fee permitted under the NASD sales charge rule. (Rule 2830(d)(3)(5)) This should create further consistency and transparency for investors and thus make their investment decisions easier. Moreover, the expense ratios of almost all mutual funds have been declining since 1990.[1] This means that today it is less costly to operate and advertise a mutual fund and consequently the need for higher marketing and distribution fees seems unnecessary.

2. The Clinic Supports the Proposed Amendments to Rule 6c-10

The amendment to Rule 6c-10 would permit funds to charge an asset-based distribution fee in excess of the 25 basis point cap imposed by new Rule 12b-2, as long as the excess charge is considered an "on going sales charge" subject to certain restrictions.

A. The Clinic Supports the Restrictions to the "On Going Sales Charge" to Protect Investors from Excessive Sales Loads

The Commission asks whether the sales charge limitations, as it proposes them, will adequately protect investors from excessive sales loads. Furthermore, the Commission asks whether the Proposed Rule will have any type of effect on the types of share classes currently offered by mutual funds. (Rule Proposal at 47-48)

The Clinic believes that the charge limitations are a good way to protect investors from excessive charges, and additionally, the restrictions should provide greater transparency and understanding of fund fees for investors. The Proposed Rule could eventually affect the types of share classes offered by funds, however, the Clinic believes that the benefits of the restrictions outweigh any possible costs.

In general, mutual funds offer three classes of shares, which have similar fees and charges across mutual funds. Class A shares will charge a front-end load, meaning that the fund charges the investor at the time the initial investment is made in the mutual fund. Class A shares have lower service fees than other share classes. Class A shares also offer break points – if the investor invests over a certain threshold money amount, he will be charged a lower upfront fee by the fund. Class B shares have either a lower initial upfront fee or have no upfront fee at all, however, mutual funds charge investors a higher annual service fee for B shares than for A shares. Class B shares will also convert to A shares after a designated period of time – this is good for investors because in A shares they will pay a lower service fee. Class C shares have no upfront sales

[1] Investment Company Institute: Research Fundamentals, *Trends in the Fees and Expenses of Mutual Funds, 2009*, Vol. 19, no. 2 (Apr. 2010)

charge, but will have the highest service fees in the fund. Usually, Class C shares will not convert to Class A or B shares.

As it stands now, an investor who does not qualify for any Class A breakpoint might find that it is better for him to invest in a Class C share that has no upfront sales load. Thus, the investor can invest the whole amount he wishes to put in the fund. However, overtime, given the higher on going sales charge on Class C shares the investor might end up paying more in fees than the Class A investor paid in the upfront fee.[2] The amendment to 6c-10 will prevent this from happening.

Under the Proposed Rule, a fund will be able to deduct an ongoing sales charge at a rate established by the fund, "provided the cumulative amount of sales charges the investor pays on any purchase of fund shares does not exceed the amount of the highest front-end load that the investor would have paid had the investor invested in another class of shares of the same fund." (Rule Proposal at 47) This provision of the Rule does not affect the 25 basis point "sales and marketing fee" described above. Mutual funds will be able to continue charging this fee, regardless of share class and regardless of whether a share class has reached its maximum allowable ongoing sales charge.

Consequently, if Class A shares have a front end load of 6.25%, then the maximum total of an ongoing sales charge, excluding the 0.25% "sales and marketing fee," that the fund could charge another class of shares would be 6.25%. For example, if another class has a front-end load of 2% then the maximum ongoing sales charge that the fund could charge that class, excluding the 0.25 "sales and marketing fee," would be 4.25%. (the 2% front end load plus the 4.25% ongoing charge equals 6.25%) The Commission explains that funds would provide an automatic conversion feature for share classes with an ongoing sales charge. These shares would automatically convert to a class without an ongoing charge once they reach the sales charge limit.

B. The Clinic is Aware of Potential Drawbacks to the Proposed Rule, However, it Believes the New Framework is Better

There are some potential drawbacks to these new restrictions, which could affect fund investors. The restrictions, imposed by the new Rules, are not in the best interests of mutual funds because the funds will be missing out on potential asset-based charges; thus funds might begin offering investors fewer choices between share classes. Moreover, the restrictions could also affect the way funds advertise and sell their shares to investors.

Under the new rules, a Class C share investor will have to convert to a Class that does not charge

[2] *See* Rule Proposal at 50-51 (explaining that an investor buying $10,000 of Class A shares with a 5% front end load would pay $500 in fees, while an investor in Class C shares with a 100 basis point asset based sales charge could end up paying $800 after 10 years and up to $2292 after 20 years).

an ongoing asset-based charge once that share class reaches the maximum charge allowed under amended Rule 6c-10 as explained above. This would not be the case today, where an investor in Class C shares will continue to pay the higher service fees as long as he remains invested in the fund. The longer the investor remains invested in Class C, the larger the discrepancy becomes between what the Class A investor paid in the front-end charge and what the Class C investor has paid in higher service fees. (Rule Proposal at 50-51)

The new Rules could push funds to offer only one share class, because in effect all share classes will now pay the same amount in asset-based charges – the only difference would be that Class A shares would pay at the outset of the investment and B and C shares would pay over time. Funds will now have an incentive to charge a front-end load on all shares, which could present a problem for smaller investors. These smaller investors will have less money to invest in the fund after the front-end charge gets deducted from their investment amount. Furthermore, having to pay an upfront sales charge will especially affect investors that only wish to invest in a mutual fund for the short term.

The Clinic believes that although these are legitimate concerns, the Proposed Rule is a definite improvement from the current framework. The Commission is, in effect, adopting a framework that is more conducive to alerting individual investors to all the information needed to make informed mutual fund investment decisions.

3. The Clinic Generally Supports the Proposed Amendments to Improve Disclosure to Investors

The Clinic generally supports the amendments to the disclosure requirements to improve the overall transparency of sales loads and asset-based distribution fees. More specifically, the Clinic applauds the Commission's focus in helping the individual investor understand the mutual fund as an investment vehicle; not only in improving fee transparency, but also in alleviating the burden of determining which share class an investor should choose to invest in.

The Commission asks whether the disclosure of situations in which choosing a certain mutual fund share class would be more advantageous than another, would be useful for investors. (Rule Proposal at 104) The Clinic believes that requiring this type of disclosure would be very beneficial for investors because it would reduce shareholder confusion and simplify the investment decision-making process. The Commission will require funds to provide a "clear description" of when it will be more advantageous for an investor to choose one share class over the other. The Commission appears to define "clear description" as identifying the actual consequences of the decision to purchase a particular share class in terms of overall loads paid and appropriate holding periods. However, the Commission doesn't go into further details of how funds should provide this information.

The Commission asks whether it should provide more specific disclosures than the ones outlined above. (Rule Proposal at 104) The Clinic believes that to maximize disclosure of information to investors, mutual funds should be required to include a table in the prospectus outlining a hypothetical investment in each of the different share classes offered by the fund. The Clinic

proposes a requirement, under the new Rules, where a mutual fund has to disclose the effects of the fees and sales charges imposed on a hypothetical $10,000 investment in each share class (the amount of the hypothetical investment would be left to the discretion of the mutual fund). The investment and fess should be projected at certain time intervals (e.g., five, ten, fifteen years, etc.). This would allow investors to determine how much of their investment would be used for an upfront sales charge, how much would go to the "marketing and service fee," and how much would go to the asset based sales charge.

Furthermore, investors would now be able to discern how the different fees and charges affect their potential return on investment. These required disclosures and examples would allow investors to make the best investment decision regarding their own circumstances.

Conclusion

The Clinic greatly appreciates the opportunity to comment on the Proposed Rule. The Clinic believes that the new disclosure requirements, as well as the restrictions on the asset-based charges, will provide investors with increased transparency of information. Additionally, the required disclosures will also provide investors with the necessary information. Moreover, the Proposed Rule is consistent with the objective of facilitating lower expenses for shareholders. Overall, the Proposed Rule represents a shift by the Commission towards a more pro-investor policy, which the Clinic strongly supports.

Respectfully Submitted,

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