

Corporate & Financial Weekly Digest

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SEC Proposes Revisions for Mutual Fund Asset-Based Fees and Broker Sales Loads

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On July 21, the Securities and Exchange Commission published a rulemaking proposal that would alter the way mutual funds impose 12b-1 fees and sales loads. The marketing and selling costs involved with running a mutual fund are commonly referred to as a mutual fund's distribution costs. To cover these costs, mutual funds are permitted to charge fees known as 12b-1 fees that are paid from the mutual fund's assets. These fees are deducted from a mutual fund to compensate securities professionals for sales efforts and services provided to the mutual fund's investors. The rule proposal would:

- *Limit "ongoing sales charges."* The proposal would limit the amount of asset-based sales charges that individual investors pay. In particular, the proposal would restrict these "ongoing sales charges" to the highest fee charged by the mutual fund for shares that have no ongoing sales charge. For example, if one class of the mutual fund charges a 4% front-end sales charge, another class could not charge more than 4% in total to investors over time. The mutual fund would keep track of how long investors have been paying ongoing sales charges. Separately, the mutual fund could continue to pay 0.25% per year out of its assets for distribution activities as "marketing and service" fees, for expenses such as advertising, sales compensation and services.
- *Enhance disclosure requirements.* The proposal would require mutual funds to identify and more clearly disclose distribution fees. In particular, a mutual fund would have to disclose any "ongoing sales charges" and any "marketing and service fees" in the mutual fund's prospectus, shareholder reports and investor transaction confirmations. Transaction confirmations also would have to describe the total sales charge rate that an investor will have to pay.
- *Allow mutual funds to sell shares through broker-dealers who establish their own sales charges.* The proposal would enable mutual funds to sell shares through broker-dealers who determine their own sales compensation, subject to competition in the marketplace. As a result, broker-dealers could establish their own sales charges, tailor them to different levels of shareholder service, and charge shareholders directly, similar to how commissions are charged on securities such as common stock. The proposal would prevent mutual funds that rely on this exemption from deducting other sales charges from mutual fund assets for that class of shares.

- *Reduce mutual fund director duties.* The proposed amendments, which would set automatic limits on mutual fund fees and charges, would eliminate the need for mutual fund directors to explicitly approve and re-approve mutual fund distribution financing plans. Directors would still have responsibility for overseeing ongoing sales charges and marketing and service fees in the same manner that they oversee other mutual fund expenses, subject to their general fiduciary duties.

The deadline for public comment on the rule proposal is November 5.

The SEC's proposing release can be found [here](#).

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