



NATIONAL ASSOCIATION OF INSURANCE
AND FINANCIAL ADVISORS

July 13, 2007

Nancy M. Morris, Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

Via Electronic Mail: rule-comments@sec.gov

Re: SEC Request for Comments on Rule 12b-1; File No. 4-538

Dear Ms. Morris:

This letter will present the views of the National Association of Insurance and Financial Advisors (“NAIFA”) in response to the Securities and Exchange Commission’s invitation to submit comments on the issues raised by Rule 12b-1.

NAIFA is a national federation of over 700 state and local associations, whose members live and work in every congressional and state legislative district. The 60,000 members of these associations are bound by NAIFA’s Code of Ethics and are full time professionals in insurance and related financial services. Founded in 1890, NAIFA is the nation’s oldest and largest trade association of insurance and financial services professionals. NAIFA’s mission is to improve the business environment, enhance the professional skills and promote the ethical conduct of agents and others engaged in insurance and related financial services that assist the public in achieving financial security and independence. Over half of all NAIFA members are licensed as registered representatives of broker-dealers and market and service mutual funds.

Our comments will focus on the following points:

- The payment of fees under Rule 12b-1 to broker-dealers and their registered representatives constitutes legitimate and appropriate compensation for providing ongoing service to their mutual fund owning clients and investors would be adversely affected if these fees were eliminated; and

- The payment of fees under Rule 12b-1 to registered representatives is an acceptable use of fund assets provided adequate disclosure is given.

1. **Rule 12b-1 fees provide legitimate, reasonable compensation to registered representatives for providing continuing service to their clients, who would be adversely impacted if these fees were eliminated.**

Most mutual fund investors use the services of a financial intermediary – a registered representative – to purchase funds. Registered representatives provide ongoing services and continuing advice to their clients regarding their investments. In return, the broker-dealer and its registered representative receive compensation as provided for under each individual fund’s 12b-1 plan.

This ongoing compensation should not be confused with commissions paid for the sale of fund shares to an investor. The sales commission paid at the time of initial purchase compensates registered representatives for different services than does the portion of Rule 12b-1 fees that serves as compensation for maintaining and servicing accounts. Compensation for the initial sale of the product is typically paid in the form of a “sales load,” which comes “off the top” of the client’s investment. Although funds have developed various options for the payment of sales loads since the advent of Rule 12b-1, registered representatives generally receive compensation for the initial sale at or near the time of sale. In contrast, payments received by registered representatives under the referenced element of Rule 12b-1 do not serve as compensation for the initial placement of the fund; rather these 12b-1 fees compensate the financial advisor for the ongoing services provided to the investor by the financial advisor after the investor becomes a client.

In accordance with NASD rules, the amount of this compensation is relatively modest: on a \$10,000 investment, the annual 12b-1 fee that is paid for providing ongoing service equals about \$25. Although the payments are small, they are an important source of income for registered representatives.

Some have questioned the propriety of funds that are closed to new investors continuing to pay 12b-1 fees. The continuing payment of these 12b-1 fees in these circumstances, however, is consistent with the overall purpose behind these fees, as this purpose has evolved over time. Registered representatives provide ongoing services to mutual fund investors. These services are provided to investors in “closed” funds as well as funds that accept new investors. The elimination of 12b-1 fees for “closed” funds would prevent registered representatives from being fairly compensated for the important, ongoing services provided to investors in such funds.

The elimination of 12b-1 fees would have a detrimental effect on the livelihoods of registered representatives. Equally important, loss of such revenues could cause funds and their distribution channels to change their ways of doing business – eliminating classes of shares, reducing payment options, and withholding ongoing services that are currently provided. This would harm not only the funds, broker-dealers and registered

representatives, but also investors, who would likely lose the advice and counsel of familiar financial services experts whom they have come to rely upon over the years.

Rule 12b-1 fees paid to registered representatives are legitimate, earned compensation for providing valuable services which greatly benefit individual investors. In exchange for a small annual payment, investors have access to a financial services expert to answer their questions and address their concerns. Without their advisor, investors would have nowhere to turn to (except for perhaps a stranger at the end of a 1-800 phone number) when they needed some reassurance in a shaky market or assistance in rebalancing their portfolios, understanding their investments and the investment choices available. If 12b-1 fees were eliminated, advisors would be forced to charge their clients either hourly or asset-based fees to compensate the advisor for the time spent servicing their clients' needs. The net effect is that while the client might save a small amount in 12b-1 fees he or she would end up paying a much larger amount in hourly or asset-based fees to receive the same service.

2. **Compensating registered representatives for providing ongoing service to the clients is a legitimate use of fund assets, provided such compensation is adequately disclosed.**

The payment of fees to registered representatives for providing ongoing service to client accounts is a legitimate and appropriate use of fund assets. When such payments are adequately disclosed, as required by law, 12b-1 fees paid for providing ongoing services pose little danger of causing conflicts of interest. Under NASD Conduct Rule 2830, 12b-1 fees are limited to a maximum of 1% of a fund's average net assets per year, including a fee of up to 0.25% to financial intermediaries for providing services or maintaining shareholder accounts. It is this latter amount that provides the "12b-1 fees" that registered representatives receive for providing ongoing service to their clients. This cap essentially eliminates the potential for conflicts of interest because registered representatives are likely to receive approximately the same percentages from all funds. Indeed, to the degree these fees provide a registered representative with any incentive at all, it would seem to be to place an investor with a fund that is likely to perform better in the long-term.

Some parties have recommended paying for ongoing client servicing out of the fund manager's fee, rather than from fund assets. This concept poses serious concerns for registered representatives. Elimination of the 12b-1 framework and allowing fund managers to pay – or not to pay – for providing ongoing servicing could have a significant adverse impact on both registered representatives and their clients. Currently, as described above, payment of 12b-1 fees for providing ongoing services is fairly uniform. Our concern is that removing fund assets from the equation and leaving it up to fund managers to pay such fees out of their own pockets will lead to the reduction or elimination of compensation for ongoing services, which could have serious consequences for investors.

In addition, payment of fees directly by fund managers, rather than out of fund assets, could lead to the very conflicts of interest (or the appearance thereof) that have concerned the Commission in past years. In order to encourage registered representatives to sell their funds, fund managers could adjust the fees paid for providing ongoing services based on fund sales. This could create an inducement for registered representatives to recommend one fund over another based on nothing more than the amount of the service fee.

In both these scenarios, the investor loses. If fund managers eliminate or reduce payments for ongoing services to the extent that providing such services is not economically feasible, registered representatives may stop providing these services and investors would lose the advice and counsel of financial services experts. If fund managers use payments of fees to induce fund sales, investors could end up investing in a fund that is not appropriate for their needs.

NAIFA believes that any concerns about the use of fund assets to pay for ongoing services provided by registered representatives could be alleviated through appropriate disclosure. Although 12b-1 fees are currently fully disclosed in standardized fee tables located at the front of every fund's prospectus, such disclosures could be revised or amended to be more transparent and understandable to the average investor. NAIFA generally supports clearer, more robust disclosure as the best way to ensure that investors understand fully the fees and expenses charged in connection with mutual fund ownership. We believe that fully informed investors would not object to their financial advisors being fairly compensated for providing beneficial services to their clients.

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In sum, NAIFA strongly supports the retention of Rule 12b-1, which both provides valuable benefits to investors and enables registered representatives to continue to receive fair compensation for the ongoing services they provide to their mutual fund-owning clients. In order to ensure that mutual fund investors fully understand the amount and purpose of fund fees and expenses, we support thorough, transparent disclosure aimed at the average investor.

Thank you for your consideration of our views. Please contact the undersigned if you have any questions regarding our comments.

Yours Truly,

/s/ Gary A. Sanders

Gary A. Sanders
Senior Counsel
Law and Government Relations