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July 13, 2007

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

Re: File No. 4-538 – Review of Rule 12b-1

Dear Ms. Morris:

Capital Research and Management Company is investment adviser to one of the largest and oldest groups of mutual funds in the nation, American Funds. We are pleased to submit these comments regarding the Commission's review of rule 12b-1. In summary, we believe that rule 12b-1 has been instrumental in expanding investor choice and is particularly valuable to small investors. We urge the Commission to consider the following points during its review.

1. Rule 12b-1 Facilitates Market-Based Innovations and Choice

Rule 12b-1 permits fund assets to be used in a transparent way for the distribution of fund shares. It was adopted in 1980 after extensive hearings by the Commission, including an administrative proceeding, that resulted in the Vanguard Group of Funds receiving permission to *permanently* devote up to .20% of the assets of its funds to pay for distribution expenses such as advertising. In 1982, the Commission recognized that it was appropriate for funds to use their assets to facilitate alternatives to front-end sales charges and began permitting funds to issue multiple share classes. In relatively short order, the mutual fund industry provided investors with a number of innovative pricing options and a cost-effective means for investors to receive ongoing service from financial advisers. Later, in recognition of these alternatives to front-end sales charges, the Commission and the NASD began applying limits specifically tailored to these situations.

These developments have broadened participation by individual investors in the financial markets and significantly contributed to addressing one of America's most urgent issues—the need to stimulate more savings and investment, particularly by individuals of modest means. At one point during the 1970s and prior to the adoption of the rule, the mutual fund industry's assets under management totaled about $30 billion. Today, even though almost two-thirds of mutual fund investors have less than $100,000 in mutual fund assets, the industry's assets under management are more than $12 trillion. We believe that the diversity of distribution options available to mutual fund investors, including those facilitated by rule 12b-1, has significantly contributed to this growth, which is all the more remarkable given the competition that mutual funds face from a variety of other investment alternatives. In light of this broader participation, repealing or materially limiting the ability of funds to use their assets to finance distribution makes little sense. It would be like eliminating or materially limiting the ability of funds to use their assets to service shareholder accounts, forcing investors to pay for these services on an individual basis. In addition, repeal would make distribution expenses less transparent and effectively increase the costs of distribution for many individual investors, as discussed below.

2. Rule 12b-1 Particularly Benefits Small Investors

Fund investors recognize the value of paying for services, including distribution-related services, on a group, "mutualized" basis. Smaller investors particularly benefit from the mutualization of these expenses in two ways: first, financial advisers are willing to service smaller mutual fund accounts because the funds provide the convenience of paying directly for shareholder servicing, rather than requiring them to establish and collect fees from many small shareholder accounts; second, the funds can establish a lower fee as a "group rate" (typically .25% annually for the service fee on class A shares) than individual shareholders are likely to be able to negotiate on their own.

In contrast, some larger and more sophisticated fund investors who require a higher level of service have elected to establish fee-based relationships with financial advisers, frequently registered investment advisers. Often, the account minimum for these types of relationships is $100,000. The average cost that is borne directly by investors in such relationships is 1.17% per year, more than a fund could pay for distribution pursuant to a rule 12b-1 plan. Because of the additional operational costs associated with providing individualized services and direct billing for these accounts, it is not economically feasible for many smaller investors to maintain fee-based accounts with their advisers, particularly when the tax disadvantages are also considered. (Service fees paid by funds are from pre-tax dollars while fees collected from the individual shareholder would be from after-tax dollars and deductible only to the extent they and other "miscellaneous expenses" exceeded 2% of income.)

The benefits of exposing a greater number of Americans to suitable investments and ongoing advice and service are clear, particularly as investors consider their retirement needs or navigate volatile markets. Not surprisingly, the vast majority of investors have expressed a clear preference for investment advice and assistance from a financial adviser. Fortunately, due to the flexibility that rule 12b-1 provides, small investors are able to compensate their financial advisers in a convenient, efficient, "mutualized" manner, resulting in lower costs for all. Our direct experience confirms the extent of service provided to shareholders by financial advisers. For example, our transfer agent, American Funds Service Company, received an average of 17,000 calls *per day* from financial advisers and their assistants in connection with their servicing of existing shareholder accounts over the last year.

In our view, regulation should accommodate the clear preferences of the marketplace whenever possible. As James Surowiecki observed in *The Wisdom of Crowds*, "Large groups of people are smarter than the elite few, no matter how brilliant—better at solving problems, fostering innovation, coming to wise decisions, even predicting the future."

3. Suggested Improvements

Although we believe that rule 12b-1 continues to provide significant benefits to individual investors, we think that two modest changes are warranted in this area. First, the guidance to mutual fund directors regarding the adoption of 12b-1 plans should be updated to better reflect the rule's own history, as well as current market realities. Second, the Commission should review its disclosure requirements regarding the use of fund assets for distribution.

a. Guidance to mutual fund directors

Although the rule itself does not restrict a board's ability to authorize the payment of any particular type of distribution expense, some argue that the guidance contained in the rule's adopting release suggests that the rule was intended to remedy only temporary distribution problems. As the discussion at the June 19, 2007 Commission roundtable regarding rule 12b-1 made abundantly clear, this argument is simply not supported by the historical record. Moreover, this guidance has almost no relevance to the exercise by fund directors of real-world business judgment. This is because distribution efforts tend to be ongoing and do not simply attempt to remedy short-term issues.

Funds most often rely on rule 12b-1 to compensate financial advisers for ongoing service to investors or as a means of providing a permanent alternative or supplement to front-end sales charges. Given that the Commission has affirmatively authorized the current use of rule 12b-1 fees for these purposes, the Commission should make it clear that the only relevant factor in adopting or reviewing a rule 12b-1 plan is whether directors have had an opportunity to exercise their business judgment.

b. Disclosure regarding distribution costs

Investors frequently complain that they are being "overwhelmed" by disclosure, much of which is not important to them. Although many investors may not have a good understanding of 12b-1 fees, this does not arise from lack of 12b-1 fee disclosure. There are multiple Form N-1A items devoted to 12b-1 fees, including a dedicated line in the fee table. Rather, this lack of understanding is the result of a disclosure regime that overwhelms investors with detail that obscures key information essential to investment decision-making. As a result, attention gets diverted from information regarding expenses that is important and understandable, such as a fund's overall expense ratio.

We believe, in general, that mutual fund prospectus disclosure could be improved through simplification. With respect to expenses, prospectus disclosure should focus investors on understanding the total cost of investing in a fund rather than requiring funds to label, often arbitrarily, individual elements of expenses. We think that emphasizing a simple, single expense ratio in the prospectus would be less confusing to investors and more properly focus them on the total expenses associated with a fund. Further detail, including disclosures regarding distribution, shareholder servicing and other expenses, could be provided in the statement of additional information.

By contrast, the Commission's current approach with respect to the disclosure of 12b-1 fees relies on labels that are difficult for investors to understand without providing meaningful guidance as to an investor's overall costs of distribution. Because investors in every fund pay for distribution in some form, whether or not the fund has a 12b-1 plan, disclosure that is overly focused on labels has proven inadequate. It makes no sense to require one fund to separately label a portion of its expenses as 12b-1 fees while simply ignoring, from a disclosure standpoint, the distribution expenses paid by other funds or investors in a different manner.

If a fund's adviser uses the profits from its investment management fee for advertisements or other activities primarily intended to result in the sale of fund shares, it is hard to see why this distribution activity should be any less transparent than distribution activities that are paid for through a 12b-1 plan. Similarly, if investors in the fund typically maintain fee-based relationships with financial advisers, the distribution expense these investors incur is every bit as material to them as a 12b-1 fee that the fund may incur in order to gain access to a fee-based platform. To ignore these types of costs, while singling out funds that provide for sales compensation, advice and service pursuant to a 12b-1 plan is to rely on labels to the detriment of providing a more comprehensive understanding of distribution costs. Focusing on the total expense ratio, although not a complete solution, would at least be a step in the right direction.

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Thank you for considering these comments. Please contact any one of the undersigned if you have questions or would like additional information.

Very truly yours,

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