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November 4, 2010

Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

RE: Proposed Mutual Fund Distribution Fees

Dear Ms. Murphy,

Waddell & Reed Financial, Inc. appreciates the opportunity to comment on the Securities and Exchange Commission's (SEC) proposed Rule 12b-2 and rule amendments that would replace Rule 12b-1 under the Investment Company Act of 1940.

Management commends the SEC for its consideration of the significant role 12b-1 fees have played in the evolution of mutual fund distribution and service by proposing the "marketing and service fee" of 25 basis points. We believe this section of the proposed rule would be enhanced if the SEC provides more clarity as to what constitutes the activities which the marketing and service fee is intended to cover.

The proposal to place a cap on sales charges in excess of 25 basis points which are designated as "ongoing sales charges", by tying the aggregate excess amount to a reference load presents certain challenges that are worth noting and should be addressed.

1. For example, currently Class C shares do not typically convert to another share class. Under the proposed rules, Class C shares would be required to convert to another share class with no more than a 25 basis point marketing and service fee. The consequences of this are likely to be:
 - a. Because of the conversion feature, some investors will be lured to Class C shares even though paying an upfront sales charge for Class A shares would be the more appropriate choice based on the amount invested and the investors' objective. The investors' actions in this regard would contradict one of the SEC's objectives with this rule change, to protect individual investors from paying disproportionate amounts of sales charges in certain share classes. Human nature being what it is, what percentage of investors would choose to pay over time versus at the point of sale? We believe a substantial percentage.

- b. Some advisors use Class C shares and the 100 basis points of 12b-1 fees to provide investment advice to less affluent investors. If those assets are converted to another share class with 25 basis point marketing and service fees those investors may no longer be economically viable to the advisors. If the investor wants to continue to get advice from an advisor, he or she would have to transfer the Class C shares to another fund complex to restart the aging on the assets or pay an additional fee separately to the advisor for advice. Otherwise, the investors would have to explore other options for getting advice.
2. The result of using the proposed “reference load” for the conversion period of shares with an “ongoing sales charge” is additional complexity for funds and broker/dealers due to the variability of maximum front end sales charges within the industry and between asset classes. In addition, to the extent different asset classes, such as equity and fixed income, have different conversion periods due to different “reference loads” the ability for shareholders to exchange shares from one asset class to another will be significantly compromised or eliminated altogether. If shares must be converted, management recommends a standard reference load for all funds such as the 6.25% upfront sales charge under NASD Conduct Rule 2830 (d)(2).
3. Certain share classes with 12b-1 fees in excess of 25 basis points (often designated as R shares) are used for 401(k) retirement plans. The 12b-1 fee structure is a convenient and efficient method for employers (plan sponsors) to pay for or contribute to plan administration costs. It is unlikely that plan sponsors or the 401(k) providers will be willing to incur the expense to develop the ability to age and convert shares as required by the proposal. In addition, if R shares are required to convert to a share class with no more than 25 basis points of fees, employers will have to look for other ways to charge plan participants for plan administration expenses or reduce benefits. Management believes the retirement share class should be exempted from converting to another class but 401(k) fee disclosure should be enhanced to increase transparency.
4. The proposed rule allows for reinvestment of dividends and distributions in a share class with an ongoing sales charge if “reinvested” shares have the same conversion schedule as the shares upon which the dividends or distributions were declared. It will be extremely difficult and expensive to relate reinvestment dividend and distribution shares to specific conversion schedules. In addition, it will be very confusing and difficult to communicate to investors. Management strongly encourages the SEC to allow the conversion of dividend and distribution reinvestments in proportion to shares being converted, a current industry practice for Class B shares.
5. In our view, the large number of funds in the industry, the multitude of share classes and variability of fee structures will make compliance with the proposed additional disclosures for transaction confirmations by broker/dealers very difficult and complex and subject to inadvertent errors. The disclosures are substantially and appropriately required prior to or at the point of sale and should remain as such rather than expanding confirmation disclosure.

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We appreciate the SEC's consideration of our comments. Please call/email if you have any questions.

Sincerely,

A handwritten signature in black ink, appearing to read "Michael D. Strohm". The signature is fluid and cursive, with a prominent initial "M" and a long, sweeping tail.

Michael D. Strohm

mds/pp