

**UNITED STATES OF AMERICA**

**Before the**

**SECURITIES AND EXCHANGE COMMISSION**

Administrative Proceedings

File No. 3-11696

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**In the Matter of**

**RS Investment Management, Inc., RS  
Investment Management, L.P.,  
G. Randall Hecht and Steven M. Cohen,**

**Respondents.**

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**PLAN OF DISTRIBUTION**

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# DISTRIBUTION PLAN FOR RS FUNDS

## Section 1 Introduction and Background

1.1 This Plan of Distribution (the "Plan") has been developed pursuant to an Order of the Securities and Exchange Commission (the "Commission") instituting administrative cease-and-desist proceedings, making findings, and imposing remedial sanctions and a cease-and-desist order in the matter of RS Investment Management, Inc., RS Investment Management, L.P. (collectively, "RS"), G. Randall Hecht and Steven M. Cohen, dated October 6, 2004 (the "Order").

1.2 Section IV.G.1 of the Order orders that RS shall pay disgorgement in the total amount of \$11.5 million and a civil money penalty in the total amount of \$13.5 million, for a total amount of \$25,000,000. Section IV.G.2 provides that a Fair Fund be established for the funds described in Section IV.G.1. The Fair Fund constitutes a Qualified Settlement Fund ("QSF") under Section 468B(g) of the Internal Revenue Code, 26 U.S.C. §468B(g), and related regulations, 26 C.F.R. §§1.468B-1 through 1.468B-5. On or before November 5, 2004, RS deposited \$13 million into an escrow account at Union Bank of California ("UBOC"). On or about December 29, 2004, RS (a) caused the assets in the UBOC account (with accrued interest) to be transferred to an escrow account at Deutsche Bank Trust Company Americas (the "DB account") and (b) deposited an additional \$6 million into the DB account. On May 24, 2005, RS deposited an additional \$6 million (the final payment) into the DB account. On or about October 5, 2005, per the instructions of Commission staff, the assets in the DB account (\$25 million, plus interest, minus taxes and fees) were transferred to the Commission's Office of Financial Management. The Fair Fund has since been deposited at the Bureau of Public Debt of the United States Treasury for investment in government obligations. Other than interest from these investments, it is not anticipated that the Fair Fund will receive additional funds, except that, as detailed in paragraph 7.1, money from other proceedings may be distributed along with the Fair Fund money.

1.3 Paragraph 29(a) of the Order stipulates that RS shall retain the services of an Independent Distribution Consultant ("IDC") acceptable to the staff of the Commission and the independent Trustees of the RS Funds, and that RS shall require the IDC to develop a Distribution Plan for the distribution of the total disgorgement and penalty ordered in paragraph IV.G of the Order, and any interest or earnings thereon (collectively, the "Fair Fund" or the "Funds Available"), according to a methodology developed in consultation with RS and acceptable to the staff of the Commission and the independent Trustees of the RS Funds. The methods of calculation of each eligible investor's share of the Fair Fund are intended by the Commission to result in a fairly estimated payment to each eligible investor that restores the impaired value of the investor's investment in the RS Funds. Some of this impaired value is susceptible to calculation, while some of this impaired value is not.

1.4 The Order stipulates (paragraph 29(a)) that the Plan shall provide for fund investors to receive, in order of priority, (i) their proportionate share of losses suffered by the fund(s) due to market timing trading activity as calculated by the IDC, and (ii) a proportionate share of advisory fees paid by the fund(s) that suffered such losses in connection with the violative trading activity. The method for determining the proportionate shareholder distribution amounts was based upon an assessment of dilution and brokerage costs.

1.5 Pursuant to the Commission Order, RS has retained Dr. Alan C. Shapiro to act as the Independent Distribution Consultant. Dr. Shapiro is the Ivadelle and Theodore Johnson Professor of Banking and Finance, Marshall School of Business, University of Southern California. Dr. Shapiro received a B.A. in Mathematics from Rice University (1967) and a Ph.D. in Economics from Carnegie Mellon University (1971). Prior to joining USC in 1978, he was an Assistant Professor at the Wharton School of the University of Pennsylvania (1971-1978). His publication credits include over 50 articles in leading academic and professional journals, several textbooks, and two monographs. Dr. Shapiro has been determined to be acceptable as the IDC by the staff of the Commission and the independent Trustees of the RS Funds. RS has agreed to pay all costs associated with the engagement of the IDC. In conjunction with Trident Consulting Group, LLC ("Trident"), Dr. Shapiro has developed a Distribution Plan. This Plan provides for the distribution of the Fair Fund among investors who held shares in ten RS mutual funds (Emerging Growth, Value + Growth, Contrarian Value, Partners, MidCap Opportunities, Internet Age, Information Age, Global Natural Resources, Diversified Growth, and Smaller Company Growth—collectively, the "ten RS Funds") between January 1, 2000, and December 31, 2003 except those investors who engaged in non-compliant trading, as defined in paragraph 2.1.1.

1.6 Dr. Shapiro has received full cooperation from the Management of RS, including access to data and individuals as requested. Dr. Shapiro is solely responsible for all work in this report. He has been assisted by Trident, which performed certain calculations and analyses under his direction. Dr. Shapiro has carried out his responsibilities using the best available data in conjunction with quantitative modeling and analysis that are based on the principles and methods of modern financial economics. Judgments regarding methodology and implementation are grounded in empirical evidence and conform to practicality constraints. Dr. Shapiro has never been employed by RS.

1.7 The IDC and the Fund Administrator (as defined in paragraph 3.1), and each of their designees, agents and assistants, shall be entitled to rely on any Orders issued in this proceeding by the Commission, the Commission Secretary by delegated authority, or an Administrative Law Judge, and may not be held liable to any person other than the Commission and the Fair Fund for any act or omission in the course of administering the Fair Fund, except upon a finding in this proceeding that such act or omission is caused by such party's gross negligence, bad faith or willful misconduct, reckless disregard of duty, or reckless failure to comply with the terms of the Plan. This limitation

on liability also applies to any order(s) to distribute additional funds in accordance with Section 8 of the Plan. Nothing in this paragraph is intended to create or restrict rights of private action and/or standing as found under the current law. This paragraph is an expression of the IDC's and the Fund Administrator's standard of care and is not intended, nor should it be deemed to be, a representation to or an indemnification of the IDC or the Fund Administrator or their designees, agents and assistants by the Commission or the Fair Fund, nor should this paragraph preclude the Commission or the Fair Fund from seeking redress from the IDC or the Fund Administrator in accordance with the rules and regulations of the Commission and the Fair Fund.

1.8 The Plan is subject to approval of the Commission and the Commission retains jurisdiction with respect to its implementation.

## **Section 2 Method for Determining Shareholder Distributions**

### 2.1 Identification of Non-Compliant Transactions

2.1.1 The IDC defined non-compliant trades as those that violated the ten RS Funds' exchange policy, as disclosed in the RS Funds' prospectus:<sup>1</sup>

Shares of one Fund may be exchanged for shares of another Fund.... However, you may not exchange your investment more than four times in any 12-month period (including the initial exchange of your investment from that Fund during the period, and subsequent exchanges of that investment from other Funds or the RS Money Market Fund during the same 12-month period).

2.1.2 The IDC identified non-compliant trades by examining the transaction history of all accounts in the ten RS Funds from 2000 through 2003. For every RS mutual fund account, the IDC constructed a time series of all exchanges between funds by matching shares in buy transactions with shares in subsequent sell transactions using the last-in-first-out (LIFO) method.<sup>2</sup> This method matched shares from the most immediate buy to shares from the most immediate sell. If the number of shares in the buy and sell transactions differed, the IDC used the minimum of the two to determine the size of the roundtrip trade. Non-compliant accounts were defined as those for which there were four or more exchanges in any calendar year between 2000 and 2003. In all accounts in which more than four exchanges took place during a 12-month period, all exchanges subsequent to the fourth exchange were considered non-compliant trades.<sup>3</sup>

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<sup>1</sup> From 2000 to mid-2003, the ten RS Funds issued a single prospectus.

<sup>2</sup> Only exchanges between RS funds were considered. Exchanges from the RS money market fund to another RS fund were considered, but purchases made from cash were not. Similarly, exchanges from an RS fund to the RS money market fund were counted, but redemptions to cash were not.

<sup>3</sup> Exchanges that were made as part of a systemic trading program (a pre-set program to invest a certain amount of money in a fund every month, for example) were not counted as exchanges for the purpose of

2.1.3 The IDC also identified a subset of non-compliant trades – those in which there was a purchase of units of a fund followed by a sale of units of the same fund within five days of the purchase. These non-compliant trades are referred to as short-term roundtrip trades. The IDC limited his estimate of dilution losses to short-term roundtrip transactions for practical reasons - expanding the damages estimate model to capture longer-term roundtrip trades would have increased the complexity of the calculations significantly. Also, the five-day window used captured more than 80 percent of all non-compliant activity in the RS Funds.<sup>4</sup> If the number of shares sold was not identical to the number bought, only the matched shares constituted the short-term roundtrip transaction. Unmatched shares may have been part of other short-term roundtrip transactions. For example, if an account purchased 500 shares of a fund on Day 1, sold 200 shares of the fund on Day 3, sold 250 shares of the fund on Day 5, and sold 50 shares of the fund on Day 7, there would be two short-term roundtrip transactions – one of 200 shares and the other of 250 shares.

## 2.2 Measurement of Dilution Losses

2.2.1 The IDC believes that the method for allocating the Fair Fund is fair and reasonable. The proportion of the Fair Fund allocated to each eligible investor is equal to that investor's proportionate share of the losses from market timing that are susceptible to calculation. The IDC calculated two types of losses – dilution costs and brokerage costs.

2.2.2 The IDC limited his estimate of dilution losses to short-term roundtrip transactions because, as discussed above, this methodology captured more than 80 percent of all non-compliant trades, and it would not have been practical to adjust the model to capture more non-compliant trades.

2.2.3 When new money comes into a fund via a short-term roundtrip transaction, it can either be invested by the fund manager, or it can remain in cash. The dilution to the fund is different under each scenario. If the money remains in cash, the value of the fund's underlying securities (and the gain or loss thereon) is the same as it would have been absent the purchase in question, but the number of units has increased. Any gain by the short-term trader is a gain that otherwise would have gone to other unit holders, and represents the dilution loss they suffered. For money that has been invested by the fund, the situation is more complicated, and it is necessary to separately examine the buy and sell sides of the short-term roundtrip trades, as explained in more detail below. Due to the different methodologies, the IDC calculated the dilution under each scenario,

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identifying non-compliant trades since they were not based on current information. The IDC also removed all exchanges that were cancelled and exchanges for less than \$100.

<sup>4</sup> For all accounts with more than four exchanges in any year between 2000 and 2003, 81 percent of purchases (weighted by dollars) and 81 percent of sales were part of short-term roundtrip transactions. Similarly, for all accounts with more than eight exchanges in any year, 81 percent of both purchases and sales were part of short-term roundtrip transactions. The percentages were also 81 percent for purchases and sales for accounts with more than 12 exchanges.

and estimated the proportion of new money that was invested on a particular day, and the proportion that remained in cash.

#### *Calculating the Day Ratio*

2.2.4 The day ratio is the percentage of cash in a fund that is invested by the fund in its securities portfolio on a particular day. The IDC estimated the day ratio by determining the cash balance at the beginning of the day, which involved adding the cash balance of the fund at the end of the previous day to the net cash flow into the fund on the previous day (since transactions are not recorded until after the end of the day). The IDC then calculated the cash investment by a fund on a given day by subtracting the cash balance at the end of that day from the cash balance at the beginning of the day. For example, if the fund had a cash balance of \$10 million at the end of day 1, net contributions of \$5 million on day 1 (which get recorded after the end of day 1), and a cash balance of \$9 million at the end of day 2, then \$6 million was invested by the fund on day 2 ( $\$10 \text{ million} + \$5 \text{ million} - \$9 \text{ million} = \$6 \text{ million}$ ). A total of \$15 million was available for investment (the original \$10 million plus the net infusion of \$5 million), so the day ratio (or percentage of available funds invested) for day 2 is 40 percent ( $\$6 \text{ million} / \$15 \text{ million}$ ). If another \$4.5 million was invested on day 3, with no net contributions on day 2, the day ratio for day 3 is 50 percent ( $\$4.5 \text{ million}$  invested out of the \$9 million available).

2.2.5 The IDC assumed that the day ratio for inflows from short-term roundtrip transactions was the same as for the fund in general. So in the example above, if a short-term roundtrip transaction resulted in \$100,000 being invested in the fund on day 1, 40 percent of this amount, or \$40,000, was assumed to have been invested the following day, 50 percent of the remaining \$60,000 was assumed invested on day 3, and so on. The fund will have available cash from the short-term trade until all of the cash has been invested, or until the short-term roundtrip transaction is completed with a sale of the fund shares.

#### *The Profit Estimate (Dilution from Infusions that Remain in Cash)*

2.2.6 For funds that remain in cash, the dilution is the profit made on the short-term roundtrip trading transaction. If the short-term roundtrip trade results in a loss, the fund benefited from the transaction, and the dilution gain to the other shareholders equals the loss to the short-term roundtrip trader.

2.2.7 To illustrate the calculation of dilution on funds that remained in cash, assume that at the end of day 0, a mutual fund had net assets of \$1,000,000, composed entirely of 50,000 shares of a stock that closes at \$20 on day 0. The fund had 100,000 units, and an NAV of \$10.00. Assume also that 10,000 units of the fund were purchased on day 0 (at the NAV of \$10.00). The next day, the sole stock owned by the fund closed at \$22. The total assets of the fund were then \$1,200,000, composed of \$1,100,000 of the stock and \$100,000 in cash. The number of units of the fund was 110,000, and the NAV

was therefore \$10.9091. The profit to the short-term roundtrip trader (assuming he sold on day 1) was \$9,091. If the short-term roundtrip transaction had not taken place, the total assets of the fund would have been \$1,100,000 (50,000 shares of the stock valued at \$22, with no cash), and the NAV of the fund would have been \$11.00 (the fund would have had 100,000 units). The dilution loss to the original fund holders was \$0.09091/unit, times 100,000 units, or \$9,091 – the exact amount of the short-term roundtrip profit.

2.2.8 The calculation of this component of dilution losses – the profit estimate on funds that remain in cash – is relatively straightforward. The IDC calculated the profit estimate as the portion of the short-term roundtrip infusion that remained in cash (which was obtained by multiplying the available funds by (1 – the day ratio)) multiplied by the one-day NAV return for the fund. This was done for each day that any cash from a short-term roundtrip infusion remained in cash. For example, if an account purchased 1,000 units of a fund on day 1 at an NAV of \$10.00, there was an infusion of \$10,000 into the fund. If the day ratio on day 2 was 0.4, \$4,000 was invested on day 2, leaving \$6,000 in cash. This amount was multiplied by the NAV return on day 2 to obtain the profit estimate for day 2. If the fund closed at an NAV of \$10.50 on day 2, the fund's NAV return would be 5.0 percent  $((10.50-10.00)/10.00)$ , and the profit estimate for day 2 would be \$300 (uninvested cash of \$6,000 times the day-2 NAV return of 5.0 percent equals \$300). If the day ratio on day 3 was 0.5, and the fund closed at an NAV of 10.605 (resulting in a next-day NAV return of 1.0 percent), the day-3 profit estimate would be \$30. The profit estimate of \$30 was computed by multiplying the available cash of \$3,000 (50% of \$6,000 remains uninvested) by the day-3 NAV return of 1.0 percent. The process was repeated for each day that any cash from a short-term roundtrip infusion remained uninvested.

#### *Buy-Side Dilution from Infusions that Are Invested*

2.2.9 To calculate the buy-side dilution for funds that were invested, the IDC multiplied the incremental amount invested that day (which equals the day ratio for that day multiplied by the remaining available funds) by the daily return to the short-term trader. For example, if the day ratio for a day was 0.5, and \$10,000 remained in a fund from the purchase portion of a prior short-term roundtrip, the incremental investment that day would be \$5,000. If the daily return of the fund on the next day was 2 percent, the buy-side dilution was \$100 (2 percent return times the incremental investment amount of \$5,000).

#### *Sell-Side Dilution from Infusions that Are Invested*

2.2.10 To calculate the sell-side dilution for funds that are invested, the IDC first determined the cumulative invested amount by summing the incremental investments made by the fund from the cash infusion by the short-term trader. If a short-term roundtrip transaction resulted in \$100,000 being invested in the fund on a day, and 40 percent of this amount, or \$40,000 was invested by the fund the following day, and 50



percent of the remaining \$60,000 was invested by the fund the next day, the cumulative invested amount after two days would be \$70,000 (\$40,000 invested the first day plus \$30,000 invested the second day). If the roundtrip was completed with a sale on day 2, \$30,000 of the original \$100,000 would still be in cash, and \$70,000 would have been invested by the fund. The IDC calculated the sell-side dilution by multiplying the cumulative investment by the next day's loss (or gain) avoided by the market-timer by selling. For example, if the fund's NAV was \$10.00 on the day of the sale, and \$9.50 on the day following the sale, the market-timer would have avoided a 5 percent next-day loss by selling. The sell-side dilution from funds invested was the cumulative investment of \$70,000 times the next-day avoided loss of 5 percent, or \$3,500. In the case of sell-side dilution, however, it was also necessary to multiply by the following adjustment factor: (number of shares outstanding before the transaction – the shares traded) divided by the number of shares outstanding before the transaction.<sup>5</sup>

2.2.11 The IDC calculated dilution costs from non-compliant trades within each account of the fund to derive a total dilution cost estimate for the fund. This calculation was done for each fund.

## 2.3 Brokerage Cost Losses

2.3.1 The IDC obtained brokerage costs for each fund for each year from 2000 to 2003 from the funds' prospectus. Brokerage cost losses stemming from non-compliant trades are calculated for each fund for each year by first calculating the cash flow invested by the fund for each day of every year of the period under review. For example, if a fund held \$10 million in cash and \$90 million in non-cash securities at the end of Day 1, and \$4 million in cash and \$96 million in non-cash securities at the end of Day 2, the cash flow for the fund on Day 2 was \$6 million. The IDC then summed all of the daily flows for the fund for every year to obtain annual investment cash flows.<sup>6</sup> These annual totals were derived without regard to whether the net cash flow on each day was positive or negative (net investment sales and purchases by the fund are each recorded as positive flows for purposes of this computation).

2.3.2 The IDC then divided the flow for each day by the annual total flow and multiplied this amount by the annual brokerage costs incurred by the fund that year to obtain a daily estimate of brokerage costs. For example, if the annual investment cash flow for a fund was \$100 million, its annual brokerage costs were \$10 million, and the cash flow on a given day was \$5 million, the brokerage cost estimate for that day would be \$500,000 ( $\$10 \text{ million} * \$5 \text{ million} / \$100 \text{ million}$ ).

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<sup>5</sup> The adjustment factor is necessary to account for the number of fund units being smaller as a result of the redemption.

<sup>6</sup> In this paragraph, the term "flows" refers to flows between cash and portfolio securities within a fund, arising from the purchase and sale of securities by the fund manager, rather than flows in and out of the fund arising from purchases and sales of fund units by investors.

2.3.3 The IDC then calculated the brokerage cost losses imposed by non-compliant trades by dividing the non-compliant exchange cash flow by the total cash flow for that day and multiplying by the daily brokerage cost estimate. For short-term roundtrip transactions, brokerage costs were only incurred by funds that were actually invested, while money that remained in cash did not result in brokerage fees. As a result, the IDC applied the day ratio to the total inflow. The IDC calculated brokerage fees for each day short-term non-compliant trading funds were invested in the fund. For long-term non-compliant trades, the IDC assumed that all inflows were invested, so brokerage costs applied to the full amount of the net flow. For example, assume that on a given day a fund had total purchases of \$10 million, total sales of \$15 million (leaving a net flow of \$5 million), total non-compliant purchases of \$2 million (of which \$1.6 million was from short-term roundtrip transactions and \$400,000 from long-term transactions), total non-compliant sales of \$3 million (of which \$1.8 million was from short-term roundtrip transactions and \$1.2 million from long-term transactions), and a day ratio of 30 percent. The net flow from long-term non-compliant transactions was therefore \$800,000 (\$1.2 million in long-term sales less \$0.4 million in long-term purchases). The net short-term non-compliant flow was \$200,000 (\$1.8 million on short-term sales less \$1.6 million in short-term purchases), of which \$60,000 was invested (\$200,000 in net flow times the day ratio of 30 percent). If the daily brokerage cost for that fund was \$100,000, the brokerage cost loss estimate for long-term non-compliant trades would be \$16,000 ( $\$0.8 \text{ million} / \$5 \text{ million} * \$100,000$ ) for that day. The short-term roundtrip brokerage cost loss estimate for that day would be \$1,200 ( $\$0.060 \text{ million} / \$5 \text{ million} * \$100,000$ ). The IDC calculated the brokerage loss for each fund for each day in this fashion.

#### *Costs by Date*

2.3.4 The IDC created a table that presents the dilution, brokerage cost, and total losses for each day during the period under review. For every day on which there was a non-compliant trade, there is a positive entry for brokerage cost losses. Similarly, for every date on which there was a non-compliant trade, there is a dilution cost estimate. This dilution cost estimate may be positive, zero, or negative, depending on whether the NAV of the fund traded rose, remained constant, or fell on the first trading day after the non-compliant trade, and whether the transaction was a sale or a purchase. There are also brokerage cost losses for days on which there was not a non-compliant trade, since, as noted above, non-compliant trades incur brokerage costs for each day the cash from the non-compliant purchase is invested, not just the first day. As a result, brokerage costs are incurred on days when no non-compliant trades occur as long as cash from short-term non-compliant trades are invested on those days.

## 2.4 Allocation of the Fund

2.4.1 The Order contemplates the distribution of the entire Fair Fund, with monies going to compensate investors, in order of priority, for (i) their proportionate share of losses suffered by the fund(s) due to market timing trading activity as calculated by the

IDC, and (ii) a proportionate share of advisory fees paid by the fund(s) that suffered such losses in connection with the violative trading activity. The IDC allocated the settlement funds in accordance with the Order by calculating the percentage of the Fair Fund that should be allocated to each investor on an account-by-account basis, with each account receiving an amount proportional to the net cost it bore from non-compliant trades, after adjusting for accounts that engaged in non-compliant trading or that had negative net costs (each of which was allocated \$0). For example, assume that total net losses are estimated at \$10,000, and the settlement fund is \$20,000. Also assume that there are only three funds (A, B, and C), and five accounts, and that the estimates of costs borne by each account in each fund are as follows, with accounts in which non-compliant trading took place highlighted.

Account	Fund A	Fund B	Fund C	Net Cost Estimate
001	\$4,000	-\$2,000		\$2,000
002		\$4,000		\$4,000
003	-\$4,000	\$1,000	\$2,000	-\$1,000
004			\$2,000	\$2,000
005	\$2,000		\$1,000	\$3,000
<b>Total</b>	<b>\$2,000</b>	<b>\$3,000</b>	<b>\$5,000</b>	<b>\$10,000</b>

2.4.2 The IDC then allocated to each account a share of the Fair Fund equal to its cost estimate as a percentage of the total cost estimate, after setting to \$0 the cost estimate of accounts in which non-compliant trading occurred, or which had a negative net cost estimate. Using the example discussed in paragraph 2.4.1, Account 003 would receive no allocation, as its net cost estimate was negative, Account 005 would receive no allocation, as it engaged in non-compliant trading, and each account's share of the settlement amount would be as follows:

Account	Net Cost Estimate	% Of Total Estimate
001	\$2,000	25%
002	\$4,000	50%
003	\$0	0%
004	\$2,000	25%
005	\$0	0%
<b>Total</b>	<b>\$8,000</b>	<b>100%</b>

2.4.3 The IDC then calculated the dollar amount of each account's allocation by multiplying its share of the total allocation by the settlement amount. In the example above, the allocation to Account 001 would be 25 percent times \$20,000, or \$5,000. Similarly, the allocation to Account 002 would be \$10,000, and the allocation to Account 004 would be \$5,000. Accounts 003 and 005 would receive no allocation.

2.4.4 The IDC set a *de minimis* distribution amount at \$10. In order to implement this *de minimis* distribution amount, the IDC applied the Gross-Up Formula. The Gross-Up Formula requires that the distributions be ranked in descending order of the size of the provisional distribution. The IDC then calculated the total amount of the distributions that were calculated to be less than \$10 (the “*de minimis* Distribution”). Beginning with the largest allocation less than \$10 and proceeding through the list, the IDC sequentially assigned a distribution of \$10 to each account until the *de minimis* Distribution was depleted. All remaining allocations were rounded down to \$0.

### **Section 3 The Tax Administrator and the Fund Administrator**

3.1 Boston Financial Data Services (“BFDS”) was the transfer agent used by RS, and, as such, was responsible for preparing and maintaining all account records for direct purchasers. The IDC has contracted with BFDS to serve as its distribution agent. As explained in paragraph 6.2, the IDC proposes that BFDS serve as the administrator of the Fair Fund (“Fund Administrator”). Under the supervision of the IDC, the Fund Administrator will be responsible for, among other things: overseeing the administration of the Fair Fund, obtaining accurate mailing information for shareholders, preparing accountings, cooperating with the Tax Administrator (identified below in paragraph 3.2) in providing the information necessary to accomplish the income tax compliance, distributing money from the Fair Fund to shareholders in accordance with this Plan, and setting up and staffing a call center to address shareholder questions or concerns regarding the distribution. RS will pay all fees of the Fund Administrator, as well as any other costs associated with the administration of the Plan of Distribution.

3.2 The Commission has appointed Damasco & Associates as the Tax Administrator (“Tax Administrator”) of the Fund. The IDC, Fund Administrator, the Bank (as defined in paragraph 5.1) and RS will cooperate with the Tax Administrator in providing information necessary to accomplish the income tax compliance, ruling and advice work assigned to the Tax Administrator by the Commission. The Tax Administrator shall be compensated by RS.

### **Section 4 Procedure for Locating and Notifying Eligible Shareholders**

#### **4.1 Locating Eligible Shareholders**

4.1.1 The Plan provides for the location and identification of eligible shareholders in several ways, depending on whether the shares were purchased directly or through a brokerage account.

### *Direct Purchases*

4.1.2 Pursuant to the Plan, the IDC will send the Fund Administrator a list of allocations to be distributed to each direct account eligible for payment. The Fund Administrator will merge this information with its records containing the name, address, and taxpayer identification number of each account holder.

### *Indirect Purchases*

4.1.3 Shares of the RS Funds were also purchased through brokerage firms. Some brokerage firms provided the RS Funds with a unique identifier for each account, rather than the name and address of each account holder. Other brokerage firms provided only "omnibus" information to the RS Funds. Under such a structure, the brokerage firm is the shareholder of record with the RS Funds, only provided aggregate daily transactions for customers to the RS Funds, and did not provide any information specific to each account to the RS Funds. The IDC will provide the Fund Administrator a list of brokerage accounts of either type for which the Plan has determined an allocation is appropriate. The Fund Administrator will request the customer name, taxpayer identification number, and last known address from these brokerage firms. The Fund Administrator will make commercially reasonable efforts to ensure the privacy and confidentiality of shareholder data by using unique account identifiers in any and all communication with RS or the IDC. The foregoing information provided by the brokerage firms shall be maintained confidentially and shared only with those parties who need to know such information for the administration of the settlement; Respondent shall not have access to any of the brokerage firm's identifying customer information.

4.1.4 For all known omnibus account holders (brokerage firms that only supplied omnibus account information to the RS Funds) with an initial distribution of \$1,000 or more and all known accounts for which a brokerage firm provided only a unique identifier, the Fund Administrator will, subject to IDC supervision, approach the brokerage firm and exercise commercially reasonable best efforts<sup>7</sup> to obtain the underlying beneficial holder data. Brokerage firms that provided a unique identifier can (1) refuse the money; (2) provide the Fund Administrator with the account data necessary for the Fund Administrator to process and distribute the allocation as determined by the IDC; or (3) use the computer algorithm underlying the allocation calculations to perform their own allocation calculations, and then make the appropriate distributions. Omnibus account holders choosing the third option will be required to certify that they used reasonable efforts in a manner satisfactory to the IDC and to the staff of the Commission in distributing money in accordance with the distribution plan. For omnibus account holders selecting the second or third option, the Gross-Up Formula will be applied to underlying account holders due to receive less than \$10. The

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<sup>7</sup> Commercially reasonable best efforts shall mean such reasonable best efforts as do not require the party, to (i) undertake extraordinary or unreasonable measures, including, without limitation, the initiation or prosecution of legal proceedings or the payment of fees in excess of normal and usual administrative fees or (ii) assume any liability or make any additional commitment.

IDC will rank distributions to underlying accounts within an omnibus account in descending order of the size of the provisional distribution and will sequentially assign a distribution of \$10 to each underlying account until the *de minimis* Distribution to that omnibus account is depleted. All remaining allocations will be rounded down to \$0. Omnibus account holders may elect more than one of these options and apply them differently in respect of different categories of beneficial holders (such as open accounts and closed accounts).

4.1.5 Omnibus account holders seeking to alter the procedures specified in paragraph 4.1.4 may apply to the Fund Administrator for permission for such alteration and the IDC will rule on such applications. The IDC may grant such applications if the requested alteration would not materially affect the distribution of funds to the contemporaneous beneficial holders.

4.1.6 Subject to the supervision of the IDC, RS will reimburse brokerage firms for commercially reasonable expenses incurred in gathering and providing the data described in paragraphs 4.1.3 and 4.1.4, as well as the cost of all communications required by the RS Plan, subject to the limitation that the amount of reimbursement will not exceed the aggregate amount of the distribution. The Fund Administrator will maintain records of efforts made to obtain the cooperation of the brokerage firms and of the responses to those efforts. After 90 days, and after the expenditure of reasonable efforts to obtain these data from brokerage firms, where all determinations as to reasonableness will be made by the IDC, the outreach program will cease. The Commission, or the Secretary of the Commission, may extend the 90-day deadline for good cause.

4.1.7 All brokerage firms providing information to the Fund Administrator or the IDC will be required to attest to the IDC that the information they are providing is true and accurate to the best of their knowledge.

4.1.8 The Fund Administrator, at the discretion and direction of the IDC, will validate/audit the data at several key points to ensure accuracy.

4.1.9 Should any investors contact the IDC or others to request a distribution, the information will be compared to the database of account numbers and allocations to ensure accurate account information and avoid duplication of payment. The request will then be forwarded to the Fund Administrator for processing.

4.1.10 The Plan requires the intermediaries of retirement accounts to distribute the monies received in accordance with their fiduciary and contractual obligations and consistent with any guidance issued by the Department of Labor.

4.1.11 In cases where the omnibus account would receive less than \$1,000 if it were treated as an individual, the omnibus provider can either refuse the distribution or apply any distribution technique that the omnibus provider, in the exercise of its reasonable

discretion, deems to be consistent with its fiduciary, contractual, or other legal obligations.

## 4.2 Notification to Shareholders and Others

4.2.1 Notice of this Plan shall be published in the SEC Docket, on the Commission website [<http://www.sec.gov>], and on RS's website [<http://www.rsinvestments.com>]. Any person or entity wishing to comment on the Plan must do so in writing by submitting their comments within thirty days of the date of the notice (i) by sending a letter to the Office of the Secretary, United States Securities and Exchange Commission, 100 F Street, N.E., Washington, D.C. 20549-1090; (ii) by using the Commission's Internet comment form ([www.sec.gov/litigation/admin.shtml](http://www.sec.gov/litigation/admin.shtml)); or (iii) by sending an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Comments submitted by e-mail or via the Commission's website should include the Administrative Proceeding File Number (Admin. Proc. File No. 3-11696) in the subject line. Comments received will be available to the public. Commenters should only submit information that they wish to make publicly available.

4.2.2 RS will provide all current shareholders of the Funds with regular and on-going updates in conjunction with their shareholder communications.

4.2.3 The Final Approved Plan and a list of frequently asked questions will be posted on a settlement website established and maintained by the Fund Administrator. The website will provide all affected shareholders with regular and ongoing updates about the Plan, including a link to the SEC website and related documents.

4.2.4 The Fund Administrator will provide customer support and communications programs which will become active at least by the time the first distribution occurs. These services will include a toll free number and a website to the public. The Commission retains the right to review and approve any material posted on the website. The IDC has contracted with the Fund Administrator to operate a customer call center. Shareholders will have the option of speaking with an individual who will be properly trained by the IDC and the Fund Administrator. Separate toll free numbers will be created for direct and omnibus account holders. These numbers will be published in the letter of explanation that accompanies the distribution check, and will be referenced on the settlement website described in paragraph 4.2.3.

4.2.5 If investors contact the IDC directly to discuss the distribution, any information received by the IDC will be provided to the Fund Administrator to ensure accurate information and avoid any duplication of payment.

4.2.6 This Fair Fund is not being distributed according to a claims-made process, so the procedures for providing notice and for making and approving claims are not applicable.

## **Section 5 Procedure for Distributing the Allocations**

5.1 The Commission has custody of the Fair Fund and shall retain control of the assets of the Fair Fund. The Fair Fund is currently deposited at the U.S. Treasury Bureau of Public Debt ("BPD"). Upon approval of the Plan by the Commission, the IDC, the Fund Administrator and Deutsche Bank Trust Company Americas ("the Bank") shall establish both an escrow account ("the Escrow Account") and a disbursement account ("Disbursement Account") at the Bank in the name of and bearing the Taxpayer Identification Number of the Qualified Settlement Fund ("QSF"). Following approval of the Plan, and submission by the IDC of a list of payees and amounts to the Commission staff, and unless otherwise directed by the Commission, the Commission staff shall cause the balance in the Fair Fund to be deposited in the Escrow Account. The Fund Administrator shall be the signer on the Escrow Account and the Disbursement Account, supervised by the IDC and subject to the continuing jurisdiction and control of the Commission. The Fund Administrator shall authorize the Bank to provide account information to the Tax Administrator. Under the supervision of the IDC, and at the direction of the Fund Administrator, the Bank shall use the assets and earnings of the Fair Fund to provide payments to distributees and to provide the Tax Administrator with assets to pay tax liabilities and tax compliance fees and costs. Funds in the Escrow Account shall be invested in either (i) AAA-rated Money Market Mutual Funds registered under the Investment Company Act of 1940 that invest in short term U.S. Treasury securities and obligations backed by the full faith and credit of the U.S. Government; provided however, that the Money Market Mutual Funds' investments in short term U.S. Treasury securities will not be made through repurchase agreements or other derivative products; or (ii) direct obligations of the United States Government of a type and term necessary to meet the cash requirements of the payments to distributees, tax obligations and fees. The IDC will receive an attestation from the Bank stating that all funds in the Escrow Account and the Disbursement Account will be held for this Plan and that the Bank will not place any lien or encumbrance of any kind upon the funds. The terms of the escrow agreement covering the Escrow Account must be reviewed and deemed not unacceptable by the staff. The Escrow Account shall be separate from the Bank's assets. All costs associated with the Escrow Account and Disbursement Account will be borne exclusively by RS.

5.2 The IDC will provide a copy of a validated list of the payees and the amounts to be disbursed to each payee (the "Issue List") to the Commission staff with the names, addresses, and tax identification numbers of eligible accountholders redacted (the "Redacted Issue List"). The IDC will certify to the Commission staff that, aside from the redactions, the Redacted Issue List is identical in all respects to the validated Issue List, which will be provided to the Bank. Upon receipt of the Redacted Issue List, the Commission staff will, as appropriate, obtain authorization from the Commission or its delegate to disburse pursuant to Rule 1101(b)(6) of the Commission's Rules on Fair Fund and Disgorgement Plans. The payees and amounts will be validated by the IDC with the assistance of the Fund Administrator through the performance of procedures and methodologies chosen by the IDC. The validation will state that the list was



