From: Zimmerman, Giff

Subject: File No. S7-41-04: Comments of Nuveen Asset Management to Proposed Amendments to Regulation M, Rel. No. 33-8511

February 15, 2005

Mr. Jonathan G. Katz
Secretary
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, DC 20549

RE: Comments of Nuveen Asset Management to Proposed Amendments to Regulation M, Rel. No. 33-8511; File No. S7-41-04

Nuveen Asset Management ("NAM") is, among other things, the investment adviser to 147 publicly-available management investment companies having approximately $63 billion in net assets as of December 31, 2004, including 110 closed-end investment companies ("CEFs") having approximately $50 billion in net assets. Each of these 110 CEFs commenced investment operations immediately after the successful completion of an initial public offering ("IPO") of its common shares. In addition, two of those CEFs have issued additional common shares pursuant to a registered and underwritten follow-on offering. Both NAM and those 110 CEFs take great interest in the proposed amendments to Regulation M, and provide comments from the perspective of CEFs and their sponsors and investment advisers.

We agree generally with the Commission's purpose behind the proposed amendments to Reg. M, as stated in the Release 33-8511: to promote the integrity and fairness of the securities offering process, and to promote price transparency during and around the time of a public offering.

We believe, however, that the Commission should take the significant differences between non-investment company issuers (which we will refer to herein as "operating companies") and investment companies, particularly those that issue shares in underwritten, non-continuous public offerings – that is, CEFs – into account when considering and adopting the final amendments to Reg. M. In particular, we believe that certain assumptions about penalty bids that the Commission made in determining to propose the blanket prohibition of penalty bids are not applicable to CEFs, that the proposed prohibition of penalty bids would demonstrably harm CEFs and their shareholders, and that the potential "troublesome issues" that the Commission believes are raised by penalty bids are either not applicable to CEFs or can be addressed by other rules that would not cause as much harm to CEFs and their shareholders as would outright prohibition.

Troublesome Issues Regarding Penalty Bids Cited by Commission. The Commission cites in Release 33-8511 three "troublesome issues" raised by penalty bids, in the text associated with endnotes 86-88:

1. Penalty bids can function as an undisclosed form of stabilization;
2. Penalty bids can induce a broker-dealer's salesperson, whose compensation in connection with the investment by a client in securities offered in a registered offering might be adversely affected if the client sells those securities during the penalty bid period, to exert improper interference with a client's right to sell those securities during the period while the penalty bid is active; and
3. There is evidence that penalty bids have been applied in a discriminatory fashion, for example by being applied to retail salespersons but not to institutional salespersons.

As we will explain below, issues #2 and #3 are effectively inapplicable to CEFs, and issue #1 can be fully addressed in the context of CEFs by enhanced disclosure.

Differences between operating companies and CEFs.

Operating companies:

a. (by definition) actively engage in businesses other than the investment in securities of other companies or issuers;
b. typically are engaged in the conduct an existing business or businesses prior to embarking on an initial public offering of securities, and issue securities in a registered public offering in order to finance the operation or expansion of those businesses;
c. determine the size of their registered securities offering primarily based on the scope of their need for such financing and only secondarily on the scope of demand for those securities, so that typically the supply of the securities will be less – sometimes far less – than the demand, and, particularly in connection with the issuance of common shares, investors and their broker-dealer representatives will have difficulty obtaining access to the desired amount of securities;
d. the fact that many IPOs are oversubscribed means that typically there is plenty of pent-up demand for the recently issued shares if such shares are sold by an initial recipient shortly after the IPO;
e. issue their securities to a mixture of institutional and retail investors; and
f. issue securities whose investment merits depend primarily on the operating results and prospects of that single company, such that the going-forward attractiveness of the securities as investments may change with company- or industry-specific events.

In contrast, CEFs:

a. do not engage in the conduct of any active business, but rather only passively and indirectly engage in business by investing in the securities issued by other companies or issuers;

b. typically have no meaningful existence prior to their initial public offering of securities, and commence investment operations only upon the completion of their registered initial public offering of securities;

c. typically will determine the size of their registered securities offering based primarily or entirely on the scope of the demand for those securities – in other words, a CEF typically will sell as many shares as the demand will reasonably allow;

d. because the number of shares issued in the fund's IPO is closely similar to the number of shares requested, there typically is no significant pent-up demand for the fund's shares to help support the price of the stock if shares are sold by an initial recipient shortly after the IPO;

e. issue their securities primarily and in many cases virtually exclusively to retail investors; and

f. issue securities whose investment merits depend primarily on (a) the operational performance of several companies or issuers and/or the investment performance of those companies' or issuers' securities, and (b) the real and/or perceived investing acumen of the fund's investment adviser.

Because of these differences, the need to be able to impose penalty bids in connection with the public offering of securities is far greater for CEFs than for operating companies, and the relative potential harm from penalty bids is significantly less. There are several reasons why.

1. In the absence of a penalty bid, a broker-dealer registered representative can effect "commission arbitrage" in a CEF common share IPO by "flipping" the shares shortly after the offering, which can greatly harm ongoing shareholders; this phenomenon is typically not applicable to operating company common share IPOs. Probably the most telling characteristic from the forgoing enumeration of differences between CEFs and operating companies is that CEFs sell as many shares as the demand will reasonably allow, which means that a broker-dealer representative is assured of being able to generate a sale and therefore a commission by simply placing an order for shares in a CEF IPO. This contrasts with an operating company IPO, where the ability to generate a commission also depends on success in receiving an allocation of the security from the syndicate and/or the representative's firm. The syndicate in a CEF common share initial public offering will typically maintain a short position by "overselling" the offering, as described in Rel. 33-8511 in the text at endnotes 65-68, and the syndicate will effect "syndicate covering purchases" for a period after the completion of the offering. In the case of all or virtually all of the common share IPOs of Nuveen CEFs, based in part on the effectiveness of these syndicate covering purchases at supporting the price of the fund's common shares, the fund's shares have traded slightly below, at or above the IPO price for an extended period after the completion of the IPO. Consequently, in the absence of the syndicate being able to impose a penalty bid, a representative could place an order to purchase the CEF's common shares in the fund's IPO for his own account or on his client's behalf, and immediately sell (or have his client sell) those shares during

the period after the completion after the IPO during which the syndicate is effecting syndicate covering purchases, with reasonable assurance that the representative could pocket all or virtually all of the commission while not bearing a significant risk that the price of the shares would decline significantly below the IPO price prior to their sale, a practice sometimes referred to a “commission arbitrage”.

This ability of the representative to pocket a commission with only a short-term outlay of funds and with little risk to principal has led, at least at certain times in the past, to wide-spread “flipping” of CEF IPO shares. Indeed, in the Nuveen funds’ experience, such flipping was a big problem for CEFs in the late 1980s and early 1990s, until CEF IPO syndicates improved the processes for identifying the representatives who had “flipped” shares and imposing the penalty bid. Even then, a penalty bid has been invoked in the vast majority of the more recent Nuveen CEF common share IPOs.

This contrasts with the experience of operating company IPOs, where to our understanding far fewer such “commission arbitrage” opportunities exist: if the IPO is a hot seller, the oversubscribed nature of the offering typically means that a registered representative cannot be assured of obtaining access to the desired number of shares in order to book the commission and then quickly flip the shares; if the IPO is not a hot seller, the representative still may not be able to access the desired number of shares, and even then the representative has no assurance that the price of the shares will be maintained at or close enough to the IPO price long enough for the representative to flip the shares at a price that enables the representative to make an assured profit. Moreover, because the operating company common shares will trade at a given moment at a price determined by the fortunes of the single issuer company and its industry in general, a broker-dealer representative attempting to engage in commission arbitrage with respect to an operating company IPO runs the significant risk that the falling fortunes of that company or industry may cause the share price to fall before the salesperson can effect or induce the sale of the shares. This may explain why, for operating companies, the penalty bid is invoked in only something like 13% of offerings (as discussed in endnote 85 of Rel. 33-8511), while the penalty bid has been invoked, in our experience, far more frequently in CEF IPOs.

2. CEFs’ common shares are designed for long-term investors, while operating company common shares are not, meaning that CEFs have a far greater need to discourage short-term flipping of IPO common shares. CEFs are designed to provide investors with the ability to have their money managed by the fund’s professional investment adviser, and to let the investment adviser make the day-to-day investing decisions. The investors effectively pay the fund’s investment adviser an advisory fee for doing so. Investors can secure the long-term benefits of that professional management only if they hold their common shares for an extended period of time. The prospectuses for every Nuveen CEF common share IPO have stated something to the effect that, “The Common Shares are designed primarily for long-term investors, and you should not view the Fund as a vehicle for trading purposes.” This contrasts with operating company common share IPOs, which do not represent a professionally managed investment designed for long-term holders and are purchased for the most part by institutions and largely self-directed

individual investors. The operating company common share IPO process comprehends that some of those investors are likely to engage in short-term trading of the common shares.

A large amount of short-term flipping of CEF common shares purchased in an IPO can be significantly harmful to long-term fund shareholders. As stated above, the size of a CEF common share IPO is determined by demand for the shares. Without the threat of a penalty bid imposed on flippers by the syndicate, a substantial and indeterminable portion of the investors in a new CEF may be flippers. Therefore, in the absence of a penalty bid, when there will be no way to discourage representatives from engaging in commission arbitrage, and there will be no way of determining in advance what portion of the investors who have placed orders to purchase shares in the IPO will be flippers, the syndicate will not be able to assure the fund that its shares will trade strongly. If a large number of common shares are bought by persons who intend to flip them shortly after the effective date, those flipped shares can overwhelm the syndicate short position, and the flood of supply of such shares into the secondary market can cause the share price to drop precipitously below the IPO price shortly after the completion of the IPO, to the detriment of those investors who intended to be long-term shareholders and did not sell shares after the IPO. The penalty bid has proven to be the only effective means of curtailing commission arbitrage in CEF common share IPOs and thereby protecting long-term shareholders from the dilution and harm that such flipping can cause.

It is our sense that if the penalty bid is prohibited in CEF registered public offerings, it will be very difficult or impossible for new CEFs to successfully conduct a public offering of their common shares without having flippers significantly impair the fund, the investment results of the ongoing shareholders, or even the viability of the CEF itself.

3. In the CEF common share IPO context, the sales commission re-allowed to the broker-dealer registered representative is designed to compensate the representative for long-term advice, and the ability of a representative to retain the commission despite flipping shares shortly after the IPO is inconsistent with that purpose. The sales commission received by a representative who places the CEF's common shares with the representative's client is closely akin to the reallowances to the representative with respect to the sale of an open-end fund. In either case, the commission reallowances is designed to compensate the representative for proving long-term advice to the client. A fairly typical re-allowance for a representative for a CEF IPO is 3.0% out of a total 4.5% underwriting spread. This contrasts with the commission re-allowance for an operating company's common share IPO, where the typical reallowances to a representative with respect to a retail client is as much as 60% of a total underwriting spread; such total spreads can reach 7% of the value of the shares sold. [In that context, the re-allowance is designed to compensate the representative as much for assisting the issuer and the underwriting syndicate with the distribution of the issuer's new securities as for any service to the investor client, and there is no common understanding that the sorts of services to the investor client even in that instance are necessarily "long-term" in nature.]

4. The three “troublesome issues” associated with penalty bids cited by the SEC in Rel. 33-8511 either do not apply to penalty bids in the CEF common share IPO process or can be remedied better by means other than prohibition.

Deferring discussion of the first cited issue to the end of this section, the second of the Commission’s recited issues was that the penalty bid may improperly interfere with a customer’s right to sell the securities in question when the customer should do so. We are not aware of any significant number of instances where an investor in a CEF common share IPO was convinced by their financial advisor/representative to defer selling shares of the CEF in order that the representative would avoid having his or her commission reclaimed. As stated above, CEFs are generally designed as long-term investment vehicles for investors (almost exclusively individuals) who seek to invest in a professionally managed investment vehicle. We believe it is unlikely that more than a very few such individuals would experience such a change in their investment needs or outlook within the typical 30- or 45-day penalty bid period that they would need to sell their new CEF common shares for their own investment-based reasons. We also are not aware of any instances in which an investor did have an investment-based reason for selling their CEF shares shortly after the IPO but that their financial advisor/representative induced them not to sell their shares until the penalty bid was removed. Our sense – admittedly based on largely anecdotal evidence – is that most selling into the market of a new CEF’s common shares within 30 to 45 days after the IPO is triggered not by individuals’ selling decisions but rather either by underwriting firms or selling group members selling shares to rid themselves of shares that had not been ultimately placed with investors, or by representatives selling shares as part of a commission arbitrage scheme. Neither of those instances represent “improper interference” with an investor’s right to sell.

The third of the Commission’s recited troublesome issues was that the assessment of penalty bids results in discriminatory effects on the ultimate customers, and in particular that the penalties were imposed on retail sales persons but not on institutional salespersons. Our experience is that CEF common shares offered in a registered public offering, unlike publicly offered operating company common shares, are purchased almost exclusively by retail investors, and so would present little or no opportunity for discrimination. Also, the firms who have served as managing underwriters of the Nuveen CEF common share IPOs have informed us that to the extent that an institutional shareholder purchased Nuveen CEF common shares in an offering and then sold their shares within the penalty bid period the firms would impose the penalty bid on the salesperson for such investor in the same manner as they would to the salesperson for a retail shareholder. We would favor a rule, similar to that proposed by the New York Stock Exchange and the National Association of Securities Dealers in SEC Rel. No. 50896, that would prohibit syndicates from imposing penalty bids in a discriminatory manner (with perhaps an allowance for demonstrable hardship situations and the like).

The first of the Commission’s recited issues was that penalty bids can function as an undisclosed form of stabilization. Given that the other recited issues are not raised to a significant extent in the CEF IPO context, and that (as discussed above) the penalty bid is the only effective means of curtailing commission arbitrage in CEF common share IPOs and thereby protecting long-term shareholders from the dilution and harm that such arbitrage can cause, it seems to us that the proper thing for the Commission to do in the final rule would be to exclude CEFs from the prohibition against penalty bids (i.e., to continue to permit penalty bids to be implemented with respect to CEFs) but to instead adopt rules requiring CEFs, selling firms and their salespersons to (a) more thoroughly disclose the details of the penalty bid to the investors, (b) state that such a penalty bid may create a conflict of interest between the salesperson's desire to retain his or her commission re-allowance and the possible need or desire of the shareholder to sell their shares, and (c) state that the existence of the penalty bid will tend to inhibit the shareholder from exercising their right to sell their shares at any time during the applicability of the penalty bid. We do not believe that such disclosure would be confusing or intimidating to investors, and would not have a chilling effect on those investors who would wish to sell their CEF common shares in the aftermarket.

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If you wish to discuss this further, please feel free to call the undersigned at xxx/xxx-xxx.

Very truly yours,

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NUVEEN ASSET MANAGEMENT