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July 27, 2006

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

Re: SR-NASD-2004-043, Proposed Rule Change Relating to Disclosure of Fees and Expenses in Mutual Fund Performance Sales Material

Dear Ms. Morris:

This letter presents the comments of Federated Investors, Inc. and its subsidiaries ("Federated")[1] on the recent issuance by the Securities and Exchange Commission ("SEC," or "Commission") of a Release approving, and seeking comments on, amendments to NASD Rules 2210 and 2211.[2] As noted in the Release, the amendments would generally require NASD member communications with the public (other than "institutional sales material" and "public appearances") that present mutual fund performance information ("performance sales material") to disclose the fund's sales charges, "total annual fund operating expense ratio," and standardized performance.

Federated is taking this opportunity to comment primarily to express its disagreement with the NASD's decision that the expense ratio must be disclosed "gross of any fee waivers or expense reimbursements" (*i.e.*, that it not reflect any current fee waivers or reimbursements). As discussed below, Federated believes that the mandated and prominent disclosure of the gross expense ratio, particularly in the context of performance sales material, would be potentially confusing to investors, and inappropriate. It would also be anti-competitive. Accordingly, Federated urges the Commission and the NASD to revise this aspect of the proposals to require instead disclosure of the fund's current expense ratio, net of fee waivers and reimbursements.

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[1] Federated Investors, Inc. is one of the largest investment management firms in the United States, managing $217.5 billion in assets as of March 31, 2006. With 140 mutual funds and a variety of separately managed accounts options, Federated provides comprehensive investment management to nearly 5,500 institutions and intermediaries including corporations, government entities, insurance companies, foundations and endowments, banks and broker/dealers.

[2] The amendments were adopted and published for comment in Release No. 34-54103, July 5, 2006; 71 FR 39379, July 12, 2006 ("Release").

Federated is aware that other commentators have previously raised very similar objections to this aspect of the NASD proposal. For example, in a letter dated September 17, 2004, to Jonathan Katz on this matter, the Investment Company Institute ("ICI") argued that "NASD should reconsider its position because the proposed approach will result in inaccurate disclosure," and that "when fee waivers and expense reimbursements are in effect, requiring disclosure of the fund's gross expense ratio in fund performance advertisements may be misleading." In Federated's view, the arguments ICI made in support of these views are compelling, and we urge the Commission to reconsider these arguments carefully.

In response to these arguments, according to the Release, NASD merely takes the conclusory position that "since fund advertisements, like prospectuses, are directed to prospective investors, any required expense ratio disclosure should not reflect fee waivers or reimbursements," without so much as even an attempt to explain why this is, or should be, so.

In point of fact, use of gross expense ratios is not self-evident; indeed, it runs counter to relevant SEC requirements. The NASD's position, phrased in this manner, seems particularly to lack a rational basis because it is the presence of fund performance data that would trigger the expense ratio disclosure requirement, yet the fund performance calculation formulas prescribed by the SEC dictate use of ***net*** expenses in making these computations. *See*, Item 21 of Form N-1A. Thus, unless this aspect of the NASD's proposal is revised, investors would see two numbers, side-by-side, that take diametrically opposed positions on the subject of fee waivers and reimbursements. Add to this the fact that, in our experience, many investors are likely to misconstrue the meaning and import of the very concept of a fund's "total annual fund operating expense ratio," and we foresee considerable misunderstanding and confusion to be the inevitable result of the NASD's decision.

We recognize that the current version of NASD's proposal would not preclude performance sales material from also presenting a fund's expense ratio net of fee waivers and reimbursements (as long as the sales material also presents the gross expense ratio, and the subsidized expense ratio is presented "in a fair and balanced manner in accordance with the standards of Rule 2210"[3]), and we expect that any fund that is benefiting from expense waivers and/or reimbursements will elect to include the net expense ratio. Indeed, arguments could be made that such a fund would have omitted material information if it did not disclose its net expense ratio.

However, in our view, disclosure of two expense ratios would only compound the concerns noted above. To us, it seems more than possible that, when faced with competing presentations of numbers with which they are relatively unfamiliar (*i.e.*, gross and net expense ratios), investors might well be inclined to ignore both of them. This would, of course, be highly ironic because, as stated in the previous SEC Release on this matter,[4] it is NASD's intention here to

[3] Even in the context of a "print advertisement," where the NASD would require the information covered by the proposals to be set forth in "a prominent text box," the current version of the proposals would permit inclusion in the text box of (as here relevant) "comparative fee data." It is our understanding that NASD would view the fund's actual, net expense ratio as an example of "comparative fee data," and therefore allow the net expense ratio to also appear in the text box.

[4] Release No. 34-50226, August 20, 2004.

"improve investor awareness of the costs of buying and owning a mutual fund." When it comes to performance sales material, investors would be much better served by disclosure of the same net expense ratio that is used to calculate the accompanying performance numbers.

More generally, this aspect of the NASD proposal neatly illustrates to us how mutual fund disclosure becomes unwieldy and opaque, to the ultimate detriment of investors. The SEC's formulas for calculating fund performance are designed to portray what a fund investor's returns actually were. Thus, fund performance figures are shown net of relevant expenses (for example, they reflect the effects of actual expenses incurred by the fund). As a result, they provide highly transparent, accurate, and above all, real information to investors. Problems arise, however, when such clarity is sacrificed in the name of some subjective regulatory goal that requires the layering on of additional (and, all too often, hypothetical) information, which is more likely to obstruct an investor's understanding than enhance it. We have little doubt that such acts of regulatory orogeny (well-intentioned as they may be) have contributed to the general perception that fund disclosure documents are not "consumer friendly."[5] In our view, the Commission now has an opportunity to take a constructive step toward promoting potentially useful disclosure, and we urge it to do so by revising the proposal to eliminate the requirement for disclosure of gross expense ratios here.

In closing, we would also point out that implementation of the NASD proposal would have anti-competitive effects. Long ago, the SEC addressed the topic of "subsidization" in connection with its proposals to standardize computation of fund performance. In adopting these measures, the SEC acknowledged commentators' observations (which remain valid today) that "subsidization benefits shareholders," and "it is usually done to help new funds with high expenses to compete with others;" in response, the SEC stated its view that "failure to disclose subsidization, where the subsidization affects performance in a material manner, would cause the advertisement to omit to state a material fact."[6] With regard to the instant matter, we think it is important to note that neither the SEC nor the NASD has asserted as a rationale any concern with funds' current practices for disclosing subsidization of fund performance. Rather, the goal has been stated in terms of "[improving] investor awareness of the costs of buying and owning a mutual fund." The fact that disclosure of actual (net) expenses would address this goal without the harmful anti-competitive effects of focusing investors' attention on gross expenses is yet another reason to revise this aspect of the proposal as we (and others) have suggested.

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[5] *See, Remarks Before the Annual Consumer Assembly*; speech by SEC Chairman Christopher Cox, Consumer Federation of America, Washington, DC, March 24, 2006.

[6] Release No. 33-6753, February 2, 1988, at section II.10.

Please contact me at 412-288-7496 with any questions about this submission.. Thank you.

Very truly yours,

Jay S. Neuman

cc: Peter Germain
Matthew Maloney