

**ATTORNEY GENERAL OF THE STATE OF NEW YORK  
BUREAU OF INVESTMENT PROTECTION**

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**In the Matter of**  
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**RS INVESTMENT MANAGEMENT, L.P.**  
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**ASSURANCE OF DISCONTINUANCE  
PURSUANT TO EXECUTIVE LAW § 63 (15)**

WHEREAS, pursuant to the provisions of the Martin Act (Article 23-A of the General Business Law), Eliot Spitzer, Attorney General of the State of New York (the "Attorney General"), commenced an investigation in August 2003 into the practices, procedures and conduct of RS Investment Management, L.P.<sup>1</sup> ("RS") during the period 1998 through September 2003 respecting market timing of mutual funds advised by RS ("the Investigation").

WHEREAS, the Investigation was conducted in cooperation with an investigation by the U.S. Securities and Exchange Commission ("SEC");

WHEREAS, RS is an investment advisor to a series of mutual funds listed in Schedule A hereto (the "Funds");

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<sup>1</sup> RS Investment Management, L.P. also refers to RS Investment Management, Inc., which acted as investment advisor to RS's then largest fund, the Emerging Growth Fund until February 2002 when RS Investment Management, L.P. assumed the advisory function for the Emerging Growth Fund. Today, both advisors are functionally the same entity with the same management. The firms are collectively referred to as "RS" herein.

WHEREAS, in the course of the Investigation, numerous witnesses were interviewed and/or deposed and extensive documentary evidence was reviewed;

WHEREAS, RS has cooperated in the Investigation by producing documentary evidence and witnesses and identifying evidence relevant to the Investigation;

WHEREAS, the Investigation revealed that certain practices by RS have violated the Martin Act, Section 349 of the General Business Law, and Executive Law Section 63(12);

WHEREAS, RS has advised regulators of its desire to resolve the Investigation;

WHEREAS, RS has agreed to reduce the management fees it charges to certain Funds distributed to retail investors in the United States, to implement certain changes with respect to the corporate governance of the Funds, to maintain a certain compliance and ethics corporate structure, and to make certain payments; and

WHEREAS, the Attorney General finds the following sanctions appropriate and in the public interest and RS agrees to the sanctions provided herein;

NOW THEREFORE, the Attorney General, based upon the Investigation, makes the following findings:

### **FINDINGS**

#### **RS's Trading Policies And Practices**

1. RS is the investment adviser to a family of ten mutual funds (the "Funds"). The Funds are equity funds with approximately \$5.1 billion in assets under management as of December 31, 2003. Between 1999 and December 31, 2003, RS's family of funds also included a money market fund. During that time, RS's Emerging Growth Fund ("the EGF") was RS's

largest fund, with approximately \$1.6 billion in assets under management as of December 31, 2003.

2. From at least 2000 through mid-2003, the ten equity Funds issued a single prospectus to potential investors. That prospectus expressly limited the number of exchanges an investor could make in and out of the Funds, stating:

#### **Exchanges**

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).

The prospectus further stated that “[e]xchange privileges may be terminated, modified, or suspended by a Fund upon 60 days prior notice to shareholders.”

3. While RS did not stringently enforce the four-exchange limitation, the firm during the relevant period took action against some customers who were excessively trading in the Funds. Such actions were usually taken against customers engaged in “market timing,” the practice of frequently buying and selling shares of the same fund, which many timers used to exploit potential inefficiencies in mutual fund pricing.<sup>2</sup> On certain occasions, RS also admonished investors to discontinue their market timing activities and stated that market timing

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<sup>2</sup> Market timing includes (a) frequent buying and selling of shares of the same mutual fund or (b) buying or selling mutual fund shares in order to exploit inefficiencies in mutual fund pricing. Market timing, while not illegal *per se*, can harm other mutual fund shareholders because it can dilute the value of their shares, if the market timer is exploiting pricing inefficiencies, or disrupt the management of the mutual fund’s investment portfolio and can cause the targeted mutual fund to incur costs borne by other shareholders to accommodate frequent buying and selling of shares by the market timer.

was not permitted in its Funds. For example, in February 2001, RS's sales department informed several investors that:

Our Firm's policy on market timing is as follows: The frequent trading of large dollar amounts in our group of Funds is disruptive to the asset base and ultimately can damage the performance of the portfolio. We do not tolerate market timers in our Funds, and we want all accounts that are market timing our Funds to be banned from market timing our Funds.

4. RS's sales department frequently used the four-exchange limitation language from the prospectuses as the basis for prohibiting market timing. Indeed, in response to a questionnaire about RS's policies and practices, RS stated: "RS Investments does not allow market timing in any funds. You may not exchange your investment more than four times in any 12-month period."

#### **Unlimited Trading and Long-Term Asset Arrangements**

5. Despite the exchange limitation provisions in the prospectuses and the internal practices described above, RS entered into at least four arrangements with three customers allowing the customers to engage in an unlimited number of trades. These arrangements included the customers' simultaneous investment of long-term assets in an RS mutual fund. The long-term assets invested generated additional management fees for RS.

6. The first of these arrangements was made in or about October 2001. At that time, an RS sales representative entered into a written agreement with a brokerage firm allowing an investor to make unlimited trades of up to \$20 million per transaction (provided that advance notice was given to RS). Simultaneously, the investor made a long-term asset commitment of \$1 million to be invested in one of the RS Funds. The asset generated approximately \$46,000 in management fees for RS.

7. By late 2002, RS had at least two other long-term asset arrangements with investors in place. These arrangements allowed the investors to engage in unlimited trading in amounts ranging from \$15 million to \$33 million per trade while at the same time investing long-term assets ranging from approximately \$2.3 million to \$5 million.

8. In the Fall of 2002, RS decided to not allow large market timers to time the EGF fund. At the time, large market timers had approximately \$80 million of market timing assets in the EGF, and the EGF's portfolio manager had requested that the market timing assets be removed from the fund. After its decision, RS began to notify its large short-term traders (who held the majority of the short-term trading assets in the fund) that they would no longer be welcome to market-time the EGF. In response, several of these frequent traders proposed to RS that they be allowed to continue their short-term trading in the EGF if they put long-term assets into the fund. One timer proposed a 2:1 ratio.

9. Despite having made a decision to not allow any large market timers in the EGF, RS decided to permit those large timers who would be willing to invest two dollars of long-term assets for each dollar of timing capacity to continue to time the Fund. One timer, Canary Capital, acting through its broker-dealer, Brean-Murray (hereinafter, "Canary")<sup>3</sup>, agreed to the 2:1 ratio, and RS agreed that Canary would be permitted to make an unlimited number of trades of up to \$65 million per transaction in return for Canary's long-term investment of \$130 million in the EGF. As to the other large timers, the then head of RS's sales staff was instructed to make sure

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<sup>3</sup> Canary Capital did not invest with RS directly, but acted through its broker-dealers, including Brean Murray and Epic Advisors. In this Assurance of Discontinuance, "Canary" means either Canary Capital itself or broker-dealers acting on Canary's behalf.

that large timers unwilling to accept a 2:1 ratio were no longer market timing in the EGF by year end, and by February of 2003, they had left the fund.

10. Between 2000 and 2003, the large investors who had timing privileges from RS netted millions of dollars of profits from timing transactions at the expense of other shareholders; Canary alone made millions between October 2002 and July 2003, again at the expense of other shareholders, from approximately 80 exchanges. RS also reaped benefits from timers: at least \$1.7 million in additional fees as a result of its arrangements with them.

11. As 2002 drew to a close, Canary was market timing the EGF and was ready to place the bulk of its required long-term investment into the Fund. If a large inflow of cash were to come from Canary on the last day of the year, however, the inflow would have the effect of increasing the amount of the Fund's uninvested cash at year end because the Fund would be unable to invest that cash in securities until after the New Year. To prevent this, an RS sales employee asked Canary's broker not to move cash into the Fund until after the end of the year so that "our Cash position won't be inflated for our year-end reporting to shareholders." An e-mail dated December 30, 2002 reporting the conversation stated:

FYI, I spoke to [a Canary employee] today approximately 1 hour before the close of the market. He wasn't anticipating a shift in their cash positions from Money Market to RS Emerging Growth, so I asked him to stay put until we get into 2003. That way, our Cash position won't be inflated for our year-end reporting to shareholders. He said it would be no problem. We don't want to restrict your trading, but we just get a little sensitive to it at the end of each quarter.

12. In early 2003, over a period of approximately one month, Canary gradually brought its long-term investment in the EGF to the agreed-upon level.

13. In May of 2003, Canary indicated it wished to reduce its long-term investment in the EGF by as much as 50% and reallocate a portion of these assets to hedge funds or another RS Fund. The then head of RS sales responded that if Canary reduced its long-term asset investment it would have to reduce its timing assets proportionally, with one adjustment: to the extent Canary invested long-term assets in a particular hedge fund, RS could agree that each long term dollar invested in the hedge fund would entitle Canary to two dollars of market timing capacity in the EGF. In addition, when Canary expressed concern that the hedge fund had a discretionary lock-up right that would be triggered if Canary's investment grew to beyond 25% of the fund's assets, RS orally agreed to not exercise the discretionary right in the event that it was ever triggered.

14. Canary invested \$10 million in the hedge fund in July of 2003, an amount not large enough to trigger the lock-up provision. The next day, Canary ceased its timing activities and withdrew all of its assets from the EGF. Thereafter, in August 2003, Canary redeemed its \$10 million investment in the hedge fund, paying the early redemption fee incurred by investors in cases of early redemption.

#### **Sharing of Confidential Portfolio Holdings Information**

15. Throughout the relevant period, RS provided information to its investors about the Funds' portfolio holdings pursuant to the following policy: RS reported its ten largest holdings ("top tens") each quarter on a 30-day lag basis (i.e., 30 days after the last day of the quarter) and its entire portfolio holdings semi-annually on a 60-day lag basis. The time lag was important to ensure that the information was stale and could not be used to the Funds' disadvantage. In

certain circumstances, RS provided its entire portfolio holdings on a more frequent basis to the research departments of certain large firms solely for research purposes.

16. Following its timing agreement with Canary, RS decided to provide Canary with the EGF's entire portfolio holdings on a more current basis than it furnished such information to other investors. Specifically, in February 2003, RS determined it would send the EGF's entire portfolio holdings to Canary quarterly with a 30-day lag instead of on a semi-annually basis with a 60-day lag. In April 2003, this policy was changed to a policy of sending Canary entire portfolio holdings monthly, with a 45- to 60-day lag.

**Failure to Disclose the Long-Term Asset Arrangements and  
the Potential Conflicts Associated With Them**

17. At no time did RS notify the Funds' shareholders and Board of Trustees that it was permitting certain investors to market time by exceeding the four-exchange language in the RS Funds while excluding others from exceeding it. RS also failed to disclose the potential conflict of interest created by RS's acceptance of long-term assets from market timers and management fees generated on those assets, contrary to the interests of other investors.

**AGREEMENT**

IT NOW APPEARING THAT RS desires to settle and resolve the Investigation, the Attorney General and RS hereby enter into this Assurance of Discontinuance, pursuant to Executive Law, 63 (15), without RS admitting or denying the Attorney General's Findings, and agree as follows:

I. **Affirmative Relief**

A. **Disgorgement and/or Restitution and Civil Penalty**

1. RS shall pay \$11,500,000 in disgorgement and/or restitution plus a civil

money penalty in the amount of \$13,500,000 for a total payment of \$25,000,000, exclusive of the value of the management fee reductions provided for in section I.C. hereof. The \$25,000,000 payment shall be remitted to and administered by the SEC in accordance with the Order Instituting Administrative and Cease and Desist Proceedings, to be issued by the SEC against RS (the "SEC Order"). Amounts ordered to be paid as civil money penalties pursuant to this Assurance of Discontinuance (*i.e.*, pursuant to the terms of the SEC Order) shall be treated as penalties paid to the government for all purposes, including tax purposes.

2. RS agrees that it shall not seek or accept, directly or indirectly, reimbursement or indemnification, including, but not limited to, payment made pursuant to any insurance policy, with regard to any or all of the amounts payable pursuant to this Assurance of Discontinuance.

3. Except as specified in Section I.E., no payments made or costs incurred by RS pursuant to or in connection with this Assurance of Discontinuance shall be borne directly or indirectly by any Fund or the shareholders thereof. RS agrees and undertakes that it and its affiliates shall not directly or indirectly assess any fee or charge to any Fund or the shareholders thereof to defray, recoup or reimburse any such payments or costs, including, but not limited to, the reduction in management fees provided for in Section I.C. below. Within 30 days after the end of RS's fiscal years 2004 through 2009, the then president or chief executive officer of RS shall certify in writing to the New York State Attorney General that RS has complied in all material respects with the provisions of this paragraph.

B. General Relief

1. RS admits the jurisdiction of the Attorney General over RS in connection

with the subject matter of the Investigation. RS will cease and desist from engaging in any acts in violation of the Martin Act, General Business Law § 349 and/or Executive Law § 63 (12) and will comply with the Martin Act, General Business Law § 349 and Executive Law § 63 (12).

2. Evidence of a violation of this Assurance of Discontinuance by RS shall constitute prima facie proof of a violation of the Martin Act, General Business Law § 349 and Executive Law § 63 (12) in any civil action or proceeding hereafter commenced by the Attorney General.

C. Reduction of Management Fee Rates For Five Years

1. RS agrees that effective January 1, 2005, RS and its Successors (as hereinafter defined in Section II.D.8) shall establish and implement reduced Net Management Fee Rates for certain of the Funds, which Funds will be identified in writing to the Attorney General on a Schedule B to this agreement within 45 days of the date of this Assurance of Discontinuance (the "Affected Funds"). "Net Management Fee Rates" means the percentage fee rates specified in the relevant agreements between RS and the Affected Funds, less waivers and reimbursements by RS, in effect as of September 30, 2004, which rates will be set forth on Schedule B. The reduced Net Management Fee Rates shall result in a reduction of \$1 million a year based upon assets under management of the Affected Funds as of September 30, 2004, for a total reduction over five years of \$5 million from the amount of fees that would have been paid by the Affected Funds based on the Net Management Fee Rates and assets under management of the Affected Funds as of September 30, 2004. RS further agrees that the reduced Net Management Fee Rates established pursuant to this paragraph shall not be increased through December 31, 2009.

2. RS represents and warrants that Schedule B will accurately and completely state: (a) assets under management by the Affected Funds as of September 30, 2004; (b) the Net Management Fee Rates for the Affected Funds as of September 30, 2004; and (c) the reduced Net Management Fee Rates and the resulting Net Management Fee reduction of \$5 million as provided in paragraph 1 above.

D. Corporate Governance of Mutual Funds

1. RS has submitted to the Attorney General certified copies of resolutions duly adopted by the Board of Trustees of each Fund in the form attached hereto as Schedule C providing that such mutual fund will comply in all material respects with the provisions of Sections I.D.2 through I.D.14. hereof during the period or periods in which such provisions are in effect under this Assurance of Discontinuance as provided for in this Assurance of Discontinuance. If any RS mutual fund amends or rescinds any such resolution or part thereof, such amendment or rescission shall be fully disclosed in the prospectus and any amendment thereto for such fund. For purposes of this subsection D, Fund includes any mutual fund into which any Fund is merged or its assets are transferred, or any reorganized mutual fund into which the assets of any Fund are transferred.

Chairman of the Board

2. The Chairman of the Board of Trustees of each Fund (the "Chairman") shall be in all respects independent of RS and its affiliates and shall have had no prior relationship (other than a purely social relationship), at any time, with RS, its then present or former affiliates, directors, officers, employees, or agents acting in their capacity as such agents, or with such Fund (other than to have been a Board member or Chairman of the Board of an RS

or RS affiliated mutual fund or closed-end fund) (hereinafter referred to as an "Impermissible Relationship"). An Impermissible Relationship includes, but is not limited to, any of the following types of relationships: (a) substantial commercial, banking or financial relationship, other than as an investor in an RS or RS affiliated mutual fund or closed-end fund on customary terms; or (b) any attorney-client, accounting, consulting, advisory, familial, charitable, employee, director, trustee or officer relationship; provided, however, a charitable relationship shall not be deemed an Impermissible Relationship if the charitable relationship is disclosed to the Board of Trustees. During the period when acting as Chairman, the Chairman and any firm with which he or she is affiliated shall have no such Impermissible Relationship. For a period of two years following conclusion of the Chairman's services as such, RS and its affiliates shall not enter into any substantial commercial, banking or financial relationship or any attorney-client, accounting, consulting, or advisory relationship with the Chairman or with any firm with which the Chairman was affiliated while Chairman; provided that nothing herein shall prevent RS and its affiliates from advising a mutual fund or a closed-end fund of which the Chairman serves as a member of the Board or of which the Chairman owns shares on customary terms. An interested person of RS or of a Fund shall not be deemed "independent." For purposes of this Assurance of Discontinuance, "interested person" has the same meaning as defined in the Investment Company Act of 1940 and "familial" means all individuals within three degrees of consanguinity or affinity.

3. In the event that RS desires input from the Attorney General as to whether a proposed Chairman of the Board of Trustees (or Senior Officer, as defined below) has a relationship that is an Impermissible Relationship, RS may make full disclosure of the facts and

circumstances and seek the prior guidance of the Attorney General; provided, however, that nothing contained herein shall be construed to excuse a breach of this Assurance of Discontinuance where a Chairman or Senior Officer has already assumed office before the input of the Attorney General was sought by RS.

Trustees

4. At least seventy-five percent of the members of a Fund's Board of Trustees: (a) shall not be interested persons, as defined by the Investment Company Act, of RS or any of its affiliates (other than a Fund); and (b) shall not have been directors, officers or employees of RS at any point during the preceding 10 years ("Independent Members"). In the event that a Fund's Board of Trustees fails to meet this requirement at any time due to the death, resignation, retirement or removal of any Independent Member, the Independent Members of such Board shall bring such Fund's Board of Trustees into compliance within a reasonable period of time not to exceed 90 days.

Senior Officer

5. Within 30 days of the parties' execution of this Assurance of Discontinuance, RS shall recommend in writing to the Board of Trustees of each Fund that the Fund appoint a full-time senior officer ("Senior Officer") with the title of at least Senior Vice President who shall have no Impermissible Relationship (as defined above) during the period he or she is acting as Senior Officer and for two years thereafter; provided, however, that the Fund's Senior Officer may be technically employed and paid by RS or an affiliate and be the same person whom the Fund designates as the Chief Compliance Officer of the Fund pursuant to Rule 38a-1(a)(4) under the Investment Company Act, 17 C.F.R. 270.38a-1(a)(4), and whom RS

designates as its Chief Compliance Officer pursuant to Rule 206(4)-7(c) under the Investment Advisers Act of 1940 (the "Investment Advisers Act"). For a period of two years following conclusion of the Senior Officer's services as such, RS and its affiliates shall not enter into any substantial commercial, banking or financial relationship or any attorney-client, accounting, consulting, or advisory relationship with the Senior Officer or with any firm with which the Senior Officer was affiliated while Senior Officer.

6. The Senior Officer of a Fund shall report directly to the Fund's Board of Trustees and such reporting shall be as often as may be appropriate, but no less than quarterly.

7. Subject to approval by the Independent Members of the Fund's Board of Trustees, the Senior Officer for such Fund shall have the authority to retain or consult consultants, experts or staff as may be reasonably necessary to assist the Senior Officer in the performance of his or her duties. The Senior Officer and such consultants, experts or staff shall be compensated at their reasonable and customary rates as determined by the Independent Trustees of the Fund. The Senior Officer may be terminated only with the approval of a majority of the Independent Members of the Fund's Board of Trustees.

8. The duties and responsibilities of the Fund's Senior Officer shall include at least the following:

(a) monitoring compliance by the Fund and its investment advisor(s) (insofar as the advisors act in connection with the Fund), with: (i) federal and state securities laws; (ii) state laws respecting potential or actual conflicts of interests; (iii) their respective fiduciary duties; and (iv) applicable codes of ethics and/or compliance manuals; and

(b) managing the process by which proposed management fees

(including, but not limited to, advisory fees) to be charged a Fund are negotiated so that such fees are negotiated in a manner which is at arms' length and reasonable and consistent with this Assurance of Discontinuance. Proposed management fees include, but are not limited to, renewal of existing management fee agreements or continuation of such existing fee agreements for more than a year after approval by a Fund's Board of Trustees.

9. The reasonableness of the proposed management fees shall be determined by the Board of Trustees of the Funds using either:

(a) an annual competitive bidding process, supervised by the Senior Officer, that includes at least three sealed bids with proposed management fees; or

(b) an annual independent written evaluation prepared by or under the direction of the Senior Officer that considers at least the following: (i) management fees (including any components thereof) charged to institutional and other clients (*e.g.*, a variable annuity that is a clone of the Fund) of RS for like services; (ii) management fees (including any components thereof) charged by other mutual fund companies for like services; (iii) costs to RS and its affiliates of supplying services pursuant to the management fee agreements, excluding any intra-corporate profit; (iv) profit margins of RS and its affiliates from supplying such services; (v) possible economies of scale as the Fund grows larger; and (vi) the nature and quality of RS's services, including Fund performance.

10. The Senior Officer of each Fund shall keep the Fund's Board of Trustees fully and promptly informed of the bidding process or the fee evaluation process, as the case may be.

11. RS shall cooperate fully and promptly with the Fund's Senior Officer and

provide any information (including preparation of summaries or other compilations of data) and documents in the possession, custody or control of RS that the Senior Officer requests and that relate to or concern any of the matters referenced in this section. RS shall promptly provide the Senior Officer with access to any director, officer or employee of RS and use its best efforts to cause such persons to answer any and all inquiries put to them by the Senior Officer that relate to or concern any such matters.

12. Each RS Fund shall: (a) appoint the Fund's Senior Officer by January 1, 2005; and (b) promptly appoint a replacement if the position of Senior Officer thereafter becomes vacant for any reason. By January 1, 2005, RS shall provide a written schedule to the Attorney General that identifies the name of the Fund's Senior Officer and describes his or her background and compensation. RS shall keep the information on the schedule current and provide an updated schedule to the New York State Attorney General within 30 days of any change in such information. For good cause shown, the Attorney General may in his sole discretion extend in writing any of the deadlines set forth in this paragraph.

13. Within 45 days of completion of the written fee evaluation provided for in Section I.D.9(b), RS shall publicly disclose a summary of such evaluation and any opinions or conclusions arising from or included in the evaluation (hereinafter referred to as the "Fee Summary"). The Fee Summary shall discuss the factors referenced in Section I.D.9(b) and sufficient specifics so that an investor in the fund can evaluate the reasonableness of the fees; provided, however, that the Fee Summary shall not be required to include or reveal confidential, competitively sensitive data, such as (but not limited to) institutional fee rates, internal costs and profit margins. Public disclosure shall include, at least: (a) continuous, prominent posting (in

downloadable format) on the Fund's website of Fee Summaries of at least the two most recent fee evaluations as part of the Fund description; (b) delivery of the Fee Summary of the most recent fee evaluation with the annual and semi-annual reports furnished to shareholders; and (c) prominent notice of the availability of the Fee Summary in the periodic account statements (if any) furnished by the Fund to individual direct investors.

14. In the event that that the Funds' Senior Officer is a person who also performs the chief compliance officer duties on behalf of RS pursuant to Rule 206(4)-7(c) under the Investment Advisers Act, then (a) the Funds' Independent Trustees shall have the sole power to hire such Senior Officer, terminate such Senior Officer, set and adjust the compensation of such Senior Officer, and exercise control over such Senior Officer; (b) RS shall have no power to hire, terminate, or set or adjust the compensation of such Senior Officer, although RS may offer, and the Funds' Independent Trustees may consider, RS's opinions and recommendations as to such decisions; (c) RS shall, at least once per every twelve months of such simultaneous service, cause an independent, outside review to be performed at RS's expense pursuant to SAS 70 or another appropriate standard with a stated focus on the independence of the Senior Officer; and (d) RS shall, at least once per every twenty-four months of such simultaneous service, cause its outside auditors to perform a review of RS's operations.

E. Disclosure to Investors

RS shall bear the costs for developing procedures, to be implemented no later than April 1, 2005, whereby RS, in an easy to understand format, shall:

1. include with each periodic account statement that a Fund sends to investors the fees and costs, in actual dollars, on a fund-by-fund basis, that would be charged to

hypothetical investments of \$5,000, \$10,000, \$25,000, \$50,000, and \$100,000 held for the next 10 years and the impact of such fees and costs on fund returns for each year and cumulatively, assuming a 5% return for each year and continuation of the reduced Net Management Fee Rates provided in section I.C. above, for disclosures made during the period through December 31, 2009, and assuming for disclosures made after December 31, 2009, a 5% return for each year and the then current Net Management Fee Rates;

2. maintain continuous, prominent posting on its website of: (a) a calculator that will enable an investor to calculate the fees and costs, in actual dollars, on a fund-by-fund basis, charged to each investor based upon the investor's most recent quarterly closing balance; and (b) the fees and costs, in actual dollars, that would be charged a hypothetical investment of \$10,000 held for the next 10 years and the impact of such fees and costs on fund returns for each year and cumulatively, assuming a 5% return for each year and continuation of the reduced Net Management Fee Rates provided in section I.C. above, for disclosures made during the period through December 31, 2009, and assuming for disclosures made after December 31, 2009, a 5% return for each year and the then current Net Management Fee Rates; and

3. Subject to SEC approval, disclose in the applicable prospectus or amendment thereto a summary showing the fees and costs, in actual dollars, that would be charged a hypothetical investment of \$10,000 held for the next 10 years and the impact of such fees and costs on fund returns for each year and cumulatively, assuming a 5% return for each year and continuation of the reduced Net Management Fee Rates provided in section I.C. above, for disclosures made during the period through December 31, 2009, and assuming for disclosures

made after December 31, 2009, a 5% return for each year and the then current Net Management Fee Rates.

II. Other Provisions

A. Scope Of This Assurance of Discontinuance

1. This Assurance of Discontinuance concludes the Investigation brought by the Attorney General and any action the Attorney General could commence against RS or any of its affiliates arising from or relating to the subject matter of the Investigation; provided however, that nothing contained in this Assurance of Discontinuance shall be construed to cover claims of any type by any other state agency or any claims that may be brought by the Attorney General to enforce RS's obligations arising from or relating to the provisions contained in this Assurance of Discontinuance. This Assurance of Discontinuance shall not prejudice, waive or effect any claims, rights or remedies of the Attorney General with respect to any person or entity not a party hereto, all of which claims, rights, and remedies are expressly reserved.

2. If RS does not make the payments as provided in section I.A. of this Assurance of Discontinuance (*i.e.*, pursuant to the SEC Order) or the Net Management Fee reductions as provided in section I.C. of this Assurance of Discontinuance, or RS defaults on any of its obligations under this Assurance of Discontinuance, the Attorney General may terminate this Assurance of Discontinuance, at his sole discretion, upon written notice to RS followed by RS's failure to cure within a reasonable time, and RS agrees that any statute of limitations or other time related defenses applicable to the subject of the Investigation and any claims arising from or relating thereto are tolled from and after December 31, 2003. In the event of such termination, RS expressly agrees and acknowledges that this Assurance of Discontinuance shall

in no way bar or otherwise preclude the Attorney General from commencing, conducting or prosecuting any investigation, action or proceeding, however denominated, related to the Investigation, against RS, or from using in any way any statements, documents or other materials produced or provided by RS after commencement of the Investigation, including, without limitation, any statements, documents or other materials provided for purposes of settlement negotiations.

3. For any person or entity not a party hereto, this Assurance of Discontinuance does not prohibit, limit or create: (a) any private rights or remedies against RS; (b) liability of RS; or (c) defenses of RS to any claims.

B. Cooperation

1. RS, its current affiliates, and its successors, assigns, and/or purchasers of all or substantially all its assets ("RS Entities") agree to cooperate fully and promptly with the Attorney General with regard to any investigation, litigation or other proceeding initiated by the Attorney General or to which the Attorney General is a party, whether pending or subsequently initiated, relating to market timing or late trading. The RS Entities shall use their best efforts to ensure that all the current and former officers, directors, trustees, agents and employees of the RS Entities and/or the Funds also fully and promptly cooperate with the Attorney General.

2. Cooperation shall include, without limitation:

(a) production, voluntarily and without service of subpoena, of all documents or other tangible evidence requested by the Attorney General and any compilations or summaries of information or data that the Attorney General requests be prepared, with the exception of any information or documents with respect to which the RS Entities have a statutory

or contractual obligation of confidentiality to persons or entities who are not parties to this Assurance of Discontinuance ("Confidential Information") and information or documents protected by the attorney-client and/or work product privileges ("Privileged Information");

(b) without the necessity of a subpoena, having the current officers, directors, trustees, agents and employees of the RS Entities attend any proceedings in New York State or elsewhere at which the presence of any such persons is requested by the Attorney General and having such current officers, directors, trustees, agents and employees answer any and all inquiries that may be put by the Attorney General to any of them at any proceedings or otherwise ("proceedings" include, but are not limited to, any meetings, interviews, depositions, hearings, trials or other proceedings), except to the extent to which such inquiries call for the disclosure of Confidential Information or Privileged Information;

(c) the RS Entities using their best efforts to cause former officers, directors, trustees, agents and employees of the RS Entities to attend any proceedings in New York State or elsewhere at which the presence of any such persons is requested by the Attorney General and to answer any and all inquiries that may be put by the Attorney General to any of them at any proceedings or otherwise, except to the extent to which such inquiries call for the disclosure of Confidential Information or Privileged Information;

(d) fully, fairly and truthfully disclosing all information and producing all records and other evidence in its possession relevant to all inquiries made by the Attorney General, except to the extent to which such inquiries call for the disclosure of Confidential Information or Privileged Information;

(e) making RS's outside counsel reasonably available to provide

comprehensive presentations concerning any internal investigation relating to all matters in this Assurance of Discontinuance and to answer questions, except to the extent to which such presentations or questions call for the disclosure of Confidential Information or Privileged Information.

3. All communications relating to cooperation pursuant to this Assurance of Discontinuance may be made to RS's attorneys as follows:

Attention: James E. Burns, Jr.  
Orrick, Herrington & Sutcliffe LLP  
405 Howard Street  
San Francisco, CA 94105  
Tel: 415-773-5700  
Fax: 415-773-5759

4. In the event that any RS Entity fails to comply with any provision of Section II.B. of the Assurance of Discontinuance, the Attorney General shall provide to RS, and any RS Entity other than RS that has failed to comply, written notice identifying the nature of the compliance failure. After receiving such notice, the non-complying RS Entity shall have seven calendar days to cure any such compliance failure identified by the Attorney General. In the event that the non-complying RS Entity fails to cure the compliance failure by the conclusion of the seven-day period, the Attorney General shall be entitled, in addition to any other remedies in the Assurance of Discontinuance or otherwise, to: (a) liquidated damages of \$100,000 from the non-complying RS Entity for each day following the seven-day period that the RS Entity remains in non-compliance; and (b) specific performance.

C. No Indemnification

1. Except as otherwise required by law or prior written agreement, RS shall

not make any payments of indemnification or allowances of expenses respecting "market timing" and "late trading" transactions to any person, including, without limitation, current or former directors, officers, employees or agents. However, any such payments by RS required by law or prior written agreement shall be payable at the time and in the manner of RS's choosing.

2. Nothing in this Assurance of Discontinuance shall prevent or limit RS from indemnifying the Funds or their successors in connection with any business combination, merger or otherwise, or from seeking remedies from persons who have practiced market timing and/or late trading in the Funds.

D. Miscellaneous Provisions

1. This Assurance of Discontinuance and any dispute related thereto shall be governed by the laws of the State of New York without regard to any conflicts of laws principles.

2. No failure or delay by the Attorney General in exercising any right, power or privilege hereunder shall operate as a waiver thereof nor shall any single or partial exercise thereof preclude any other or further exercise thereof or the exercise of any other right, power or privilege. The rights and remedies provided herein shall be cumulative.

3. RS consents to the jurisdiction of the Attorney General in any proceeding or action to enforce this Assurance of Discontinuance.

4. RS enters into this Assurance of Discontinuance voluntarily and represents that no threats, offers, promises or inducements of any kind have been made by the Attorney General or any member, officer, employee, agent or representative of the Attorney General to induce RS to enter into this Assurance of Discontinuance.

5. RS agrees not to take any action or to make or permit to be made any

public statement denying, directly or indirectly, any finding in this Assurance of Discontinuance or creating the impression that this Assurance of Discontinuance is without factual basis.

Nothing in this paragraph affects RS's: (a) testimonial obligations; or (b) right to take legal or factual positions in defense of litigation or in defense of other legal proceedings in which the Attorney General is not a party.

6. This Assurance of Discontinuance may be changed, amended or modified only by a writing signed by all parties hereto.

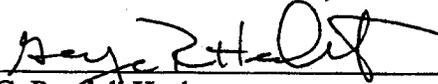
7. This Assurance of Discontinuance, together with the attached schedules, constitutes the entire agreement between the Attorney General and RS and supersedes any prior communication, understanding or agreement, whether written or oral, concerning the subject matter of this Assurance of Discontinuance.

8. This Assurance of Discontinuance shall be binding upon RS and its successors, assigns, and/or purchasers of all or substantially all its assets ("Successors") for as long as RS or any Successor continues to provide investment advisory services to the Funds or any successors thereof (including any funds with which a Fund is merged or its assets are transferred, or any reorganized mutual fund into which the assets of any Fund are transferred) provided, however, that any Successor to RS may petition the Attorney General and obtain relief from such undertakings.

9. This Assurance of Discontinuance shall be effective and binding only when this Assurance of Discontinuance is signed by all parties. This Assurance of Discontinuance may be executed in one or more counterparts, each of which shall be deemed an original but all of which together shall constitute one instrument.

WHEREFORE, the following signatures are affixed hereto on the dates set forth below.

RS INVESTMENT MANAGEMENT, L.P.

By: 

G. Randal Hecht  
Chief Executive Officer  
RS Investment Management, L.P.

Dated: October 5<sup>th</sup>, 2004

ELIOT SPITZER,

Attorney General of the State of New York

By: 

Roger L. Waldman, Esq.  
Senior Enforcement Counsel  
Investment Protection Bureau

Dated: October 6, 2004

ACKNOWLEDGMENT

STATE OF California

:SS.

COUNTY OF San Francisco

On this 1<sup>st</sup> day of October, 2004, before me personally came George <sup>HECHT</sup>, ~~known to~~

me, who, being duly sworn by me, did depose and say that he is George <sup>HECHT</sup> of

RS Investment Mgmt L.P., the entity described in the foregoing Assurance of Discontinuance, is duly authorized by RS Investment Mgmt L.P. to execute the same, and that he signed his name in my presence by like authorization.

Notary Public

My commission expires: 21 June 2007

Dated: October 1<sup>st</sup>, 2004



## **SCHEDULE A**

RS Diversified Growth Fund

RS Emerging Growth Fund

RS Growth Fund

The Information Age Fund

RS Internet Age Fund

RS MidCap Opportunities Fund

RS Smaller Company Growth Fund

RS Contrarian Value Fund

RS Global Natural Resources Fund

RS Partners Fund

**SCHEDULE B**

**[TO BE PREPARED IN ACCORDANCE WITH SECTION I.C.]**

## SCHEDULE C

WHEREAS, RS Investment Management, L.P. and the Attorney General of the State of New York ("Attorney General") are proposing to enter into an Assurance of Discontinuance Pursuant to Executive Law Sec. 63(15) ("Assurance of Discontinuance"); and

WHEREAS, paragraphs 1 through 14 under Section D, captioned "Corporate Governance of Mutual Funds" in the Assurance of Discontinuance provide for each of the RS mutual funds listed in Schedule A hereto ("Funds") to comply with the requirements of corporate governance set forth therein (the "Corporate Governance Requirements");

NOW, THEREFORE, to provide assurance to the Attorney General of the compliance of the Funds with the Corporate Governance Requirements, the Board of Trustees of each of the Funds hereby adopts the following resolutions:

RESOLVED, that the Fund will comply in all material respects with the Corporate Governance Requirements during the period or periods in which such provisions are in effect under the Assurance of Discontinuance; and

FURTHER, RESOLVED, that the foregoing resolution shall remain in effect until amended or rescinded by the vote of at least 80% of all incumbent members of the Board of Trustees of the Fund at the time of such amendment or rescission.