

MEMO# 3919

July 9, 1992

VERMONT COMMENTS ON FUND LIABILITY FOR TELEPHONE TRANSACTIONS

July 9, 1992 TO: STATE SECURITIES MEMBERS NO. 33-92 TRANSFER AGENT ADVISORY COMMITTEE NO. 34-92 RE: VERMONT COMMENTS ON FUND LIABILITY FOR TELEPHONE TRANSACTIONS _____ The Vermont Securities Division recently began issuing comments with respect to language in fund prospectuses relieving the fund or its affiliates of any liability for acting upon instructions in connection with telephone redemptions or exchanges. It is our understanding that such disclosure is fairly common in prospectuses and/or account applications. An example of the language that the staff of the Vermont Securities Division has objected to is: Neither the Fund nor the Transfer Agent will be responsible for acting upon any instructions believed by them to be genuine. According to the comment letter issued by the Division (samples attached), the staff is concerned that a fund may not have implemented procedures to ensure the authenticity of the caller and/or transaction. The letter is somewhat confusing in that it implies that a fund should be held strictly liable for investor losses but also states that funds should be responsible for transfers which occur because of the transfer agent's "negligence or failure to perform its fiduciary duties." The Institute contacted the Director of the Division to seek clarification of the Division's comments. According to the Director, Vermont is not taking the position that funds should be held strictly liable for telephone transactions. Rather, a fund should be responsible for losses due to negligence. Moreover, a fund receiving this comment letter from the Division should submit a response outlining the fund's procedures with respect to telephone transactions which includes the safeguards the fund has adopted to protect against fraudulent transactions (e.g., testing the identity of the caller by requiring the caller to state an identification number or some other information that would be known only by the shareholder or refusing to send the redemption proceeds to an address that is not the shareholder's address of record). By doing so, the fund will not be required to "sticker" the prospectus for Vermont. Inasmuch as it is our understanding that several states have expressed concern with respect to telephone disclaimers, the Institute contacted the NASAA Investment Company Registration/Trading Practices Committee. The Institute will be submitting a detailed letter to the NASAA Committee, and appropriate states, outlining the legal basis for such disclaimers as well as the safeguards funds have adopted to protect shareholders in the very near future. We will keep you advised of developments. Patricia Louie Assistant Counsel Attachments

abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice.