

MEMO# 19756

February 17, 2006

Harvard Paper on T+1 Accounting

©2006 Investment Company Institute. All rights reserved. Information may be abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice. [19756] February 17, 2006 TO: ACCOUNTING/TREASURER COMMITTEE No. 2-06 BOARD OF GOVERNORS No. 9-06 PUBLIC COMMUNICATIONS COMMITTEE No. 3-06 RE: HARVARD PAPER ON T+1 ACCOUNTING As you know, Harvard Business School Professor Peter Tufano has authored a new study highly critical of the widespread method for calculating daily NAVs, known as "T+1 accounting." The paper, entitled "Live Prices and Stale Quantities: T+1 Accounting and Mutual Fund Mispricing" is attached. The study was featured in Mark Hulbert's column in the New York Times on Sunday Feb. 12. It has also been discussed in several trade press articles. In addition, Prof. Tufano was a panelist this week at the annual conference of the Mutual Fund Directors Forum in Washington. There is potential for further media coverage of this issue in coming weeks. The study uses data for 26 funds from an unspecified group of fund companies. Using this information, it calculates the percentage of times that the funds' NAVs would have differed by more than a penny if they had used T+0 portfolios. For this group of funds, the study concludes that the NAVs would have been different by more than a penny between 2 and 20 percent of the days, depending on the fund, even though on average the difference between the two measures is zero. While the paper points out how T+1 and T+0 accounting may create different NAV calculations, its sample of funds is small and is not necessarily representative of the industry as a whole. Furthermore, it does not discuss the feasibility or costs associated with moving to a T+0 accounting regime. It does note that these issues could only be addressed with a cost-benefit analysis. We have disseminated discussion points for use in replying to media inquiries, which are also attached. They essentially make the point that T+1 accounting is well-established, is fully in accordance with SEC regulation, and has consistently worked well and without major incident for many years. We also pointed out the difficulty of manipulating the system against shareholder interests, noting that insiders are subject to very tight compliance procedures which include pre-clearance and close monitoring of insider trades in fund shares. 2 We intend to keep a close eye on media coverage of this issue and we are exploring further research of this issue with several member firms. We have also initiated discussions with the authors of the study. As always, please contact me with any questions or concerns. F. Gregory Ahern Chief Public Communications Officer Attachment (in .pdf format)