

MEMO# 3336

December 10, 1991

INSTITUTE RESPONDS TO NASAA INVESTOR ALERT ON MUTUAL FUNDS

December 10, 1991 TO: BOARD OF GOVERNORS NO. 87-91 STATE SECURITIES MEMBERS
NO. 53-91 CONTRACTUAL PLANS COMMITTEE NO. 19-91 RE: INSTITUTE RESPONDS TO
NASAA INVESTOR ALERT ON MUTUAL FUNDS

In October, the North American Securities Administrators Association, Inc. ("NASAA") and the Council of Better Business Bureaus ("CBBB") jointly issued an Investor Alert regarding investing in mutual funds. The Alert describes briefly the nature of mutual funds, discusses potential problems for mutual fund investors and provides ten tips on buying mutual funds. However, as well as providing useful information, the Alert also contains numerous misleading statements with respect to mutual funds. For example, the Alert constantly refers to "hidden fees" and "unexpected commissions" that may be assessed by a fund, but fails to mention that Form N-1A requires all fees to be clearly disclosed in a fee table which is required to be included in the front of a fund's prospectus. In addition, the Alert states that "some mutual funds and sales organizations do little or nothing to inform potential investors that the SAI exists," but fails to state that Form N-1A requires that disclosure be included on the cover page of a fund prospectus regarding the availability of the SAI. The Alert also cautions investors against making an investment decision based on advertisements and sales literature since such information is not reviewed by the SEC before it is used. However, the Alert fails to state that investors cannot purchase shares of a mutual fund off an advertisement and that most sales literature and advertising is reviewed by the NASD. The Institute contacted the Executive Director of NASAA to object to the Alert's misleading characterization of the fund industry and was subsequently informed that the Alert would no longer be distributed by NASAA. In addition, the Institute submitted a letter to the President of NASAA which detailed its objections to the overall tone and specific allegations contained in the Alert. The Institute's letter expressed concern over the need to issue an Investor Alert on mutual funds by noting that in the past, Investor Alerts had been issued on topics such as boiler room scams, international investment frauds, penny stock frauds, "dirt pile" gold swindles and pyramid scheme frauds. The Institute objected to the implication that, by issuing this Alert, NASAA has determined that investing in mutual funds is in that same category of "investment fraud." The Institute's letter also objected to several of the more egregious misleading statements contained in the Alert (such as those listed above). The letter concluded by noting that the issuance of dire warnings by state regulators is bound to discourage investors from purchasing mutual fund shares, encourage redemptions and lead to a general loss of confidence in the fund industry. Moreover, scaring investors off mutual funds may lead investors to products that are less suitable, far less regulated and much more susceptible to abuse -- the very products that are the legitimate focus of NASAA Alerts. * * * A copy of the Institute's letter, the NASAA Investor Alert and a press release

issued by the Idaho Securities Bureau is attached. We will keep you informed of developments. Patricia Louie Assistant General Counsel Attachments

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