INVESTMENT COMPANY INSTITUTE

MEMO# 1862

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DIVISION OF INVESTMENT MANAGEMENT RESPONDS TO INSTITUTE'S PROPOSED UNIFORM PERFORMANCE ADVERTISING RULES FOR UNIT INVESTMENT TRUSTS

- 1 - April 27, 1990 TO: UNIT INVESTMENT TRUST COMMITTEE NO. 19-90 RE: DIVISION OF INVESTMENT MANAGEMENT RESPONDS TO INSTITUTE'S PROPOSED UNIFORM PERFORMANCE ADVERTISING RULES FOR UNIT INVESTMENT TRUSTS ____ The Institute has received a response from the SEC's Division of Investment Management to our December 7, 1989, submission proposing uniform performance advertising rules for unit investment trusts. (See Memorandum to Unit Investment Trust Members No. 67-89, dated December 11, 1989.) The response (a copy of which is attached) includes a staff memorandum, setting forth its analysis of, and questions relating to, the Institute's proposal. The memorandum reiterates the staff's position that internal rate of return ("IRR") provides the best measure of unit investment trust performance. The memorandum asserts that the Institute's proposed estimated long-term return ("ELTR") formula consistently generates yield figures that are higher than IRR for the same portfolios. The Division attributes this difference to the treatment of sales load and compounding of - 2 - yield under the ELTR formula. The memorandum argues that it is inappropriate for unit trusts to follow the approach taken by the mutual fund yield formula in these areas because trusts have a fixed life and do not reinvest dividends. In addition, the memorandum questions the failure to include a time-weighting component. The Division's memorandum also questions the Institute's proposed second alternative for treatment of accretion of market discount with respect to tax-free obligations (which would permit inclusion of this component, provided additional disclosures were made). It further suggests that unit investment trusts with portfolios consisting of more than a de minimis amount of variable rate debt should not be permitted to quote a forward-looking performance figure such as ELTR. Finally, the memorandum notes that the use of IRR would obviate the need for a separate formula, such as that proposed by the Institute, to calculate the yield of unit investment trusts whose shares are held by other unit investment trusts. The Division of Investment Management has indicated that it will bring a rule proposal relating to unit investment trust performance before the Commission this summer. Accordingly, the staff's letter requests that we respond to their questions - 3 - by June 1. They have subsequently agreed to extend this deadline until July 1. We will circulate a draft response to the Committee as soon as possible. Frances M. Stadler Assistant General Counsel