



INVESTMENT
COMPANY
INSTITUTE

SUMMARY OF RESEARCH FINDINGS

THE PROFILE PROSPECTUS: AN ASSESSMENT BY MUTUAL FUND SHAREHOLDERS

*Report to the U.S. Securities and Exchange Commission by
the Investment Company Institute—May 1996*

Background

In October 1994, Arthur Levitt, Jr., Chairman of the U.S. Securities and Exchange Commission (SEC), launched an innovative project to improve disclosure about mutual funds. He called upon mutual fund companies to develop a concise or “profile” prospectus that would contain information essential to an investment decision. In response to Chairman Levitt’s initiative, the Investment Company Institute¹ and eight mutual fund groups,² in consultation with the SEC’s Division of Investment Management and with the Investment Companies Committee of the North American Securities Administrators Association (NASAA), developed a prototype of a profile prospectus that established 11 critical areas to be addressed in fund disclosure:

1. the fund’s goals or objectives;
2. its investment strategies;
3. its risks;
4. the kind of investors for whom the fund might be an appropriate investment;
5. a table showing fees and expenses of the fund;
6. a graphic depiction of the variability of the fund’s performance over time, in the form of a bar chart presenting the fund’s total return in each of the last ten years, accompanied by standardized SEC performance data of the fund;
7. the name of the fund’s investment adviser;

8. how investors may purchase shares of the fund, including any minimum investments;
9. how investors may redeem their shares;
10. when and how distributions are made by the fund; and
11. other services the fund offers to investors.

In August 1995, the SEC approved use of prototype versions of the profile prospectus for a one-year trial period. Participating fund groups have developed profile prospectuses for 38 equity, bond, and money market funds and provided them to prospective investors. In addition, the Institute and fund groups participating in the project have undertaken research to determine how shareholders assess the profile prospectus. The research methods and results are summarized below. This research represents, to the Institute’s knowledge, the most extensive survey ever conducted of U.S. investors regarding the content and format of mutual fund disclosure.

Research Methods

The Institute undertook research to determine whether the profile prospectus provides the information that investors seek before purchasing a mutual fund and whether the profile prospectus enables investors to obtain key investment information more readily than the prospectus currently in use (the Section 10(a) prospectus).

¹ The Investment Company Institute is the national association of the U.S. investment company industry. Its membership includes 5,876 open-end investment companies (“mutual funds”), 448 closed-end investment companies, and 10 sponsors of unit investment trusts. Its mutual fund members had assets of \$2.994 trillion as of March 31, 1996, accounting for approximately 95 percent of total industry assets, and had over 38 million individual shareholders in mid-1995.

² The eight fund groups are American Express Financial Corporation; Bank of America N.T. & S.A.; Capital Research and Management Company; The Dreyfus Corporation; FMR Corp. (Fidelity); Scudder, Stevens & Clark, Inc.; T. Rowe Price Associates, Inc.; and The Vanguard Group, Inc.

The Institute engaged Response Analysis Corporation, an independent research firm, to conduct in-person interviews with over 1,000 randomly selected shareholders who had purchased at least one mutual fund in the preceding five years. Each recent buyer read a profile prospectus and a Section 10(a) prospectus for comparable types of mutual funds within the same fund family and evaluated and compared a number of features of the two prospectuses.

In addition, various fund groups participating in the profile prospectus initiative undertook research with their customers and, in some instances, with financial advisers to gauge the usefulness and effectiveness of the profile prospectus.³ Each of the fund groups undertook quantitative research, but their approaches varied considerably. For example, some fund groups conducted surveys with randomly selected prospective investors who had been sent a profile prospectus along with a Section 10(a) prospectus and other fund materials. These prospective investors were asked to compare the features of the profile and Section 10(a) prospectuses. Another fund company surveyed a random sample of its shareholders and financial advisers through whom its funds are sold. Still another company interviewed a randomly selected sample of brokers who had sold a substantial volume of the company's funds in 1995.

Research Results

The studies conducted by the Institute and its members provide important information about the needs of fund shareholders and the potential of the profile prospectus to serve as a model for effective disclosure. The research findings are presented in a two-volume report, *The Profile Prospectus: An Assessment by Mutual Fund Shareholders*, submitted to the SEC by the Institute on May 20, 1996. Volume I contains the results of the Institute's survey. Volume II contains the results of the research undertaken by Institute members.

As SEC Chairman Levitt observed in August 1995, research of this kind should help the Commission determine “what, if any, permanent changes to fund disclosure should be made” and “whether investors should be able to rely on a stand-alone profile...in deciding to invest in funds.”⁴ In light of the research findings summarized below, the Institute has recommended that the SEC propose rulemaking that would authorize the use of the profile prospectus, with enhancements to the prototype, and subject to strict conditions governing future use.⁵

The principal research findings by the Institute and participating fund groups are as follows.

1. The Section 10(a) prospectus is not meeting the needs of many investors for making investment decisions.

- **Many investors do not use or read the Section 10(a) prospectus.** Half of all recent fund investors surveyed by the Institute did not consult or use the Section 10(a) prospectus for *any* purpose before making their most recent purchases of a mutual fund.⁶ Most investors who made no use of the Section 10(a) prospectus expressed a lack of a full understanding of mutual fund investing.
- **Investors find the Section 10(a) prospectus to be neither easy to use nor easy to understand.** In the Institute's survey, fewer than 36 percent of all respondents reported that it was very easy locating or understanding key investment items in the Section 10(a) prospectus. Investment risk posed the greatest challenge, with little more than one fifth saying that locating or understanding the risk information was very easy (Figures 1 and 2).

³ Six of the eight participating fund groups conducted quantitative research on the profile prospectus, all of the results of which research are included in the Institute's report to the SEC.

⁴ Remarks by Chairman Levitt at a press conference to announce the distribution of the profile prospectus to investors (July 31, 1995).

⁵ See letter from Paul Schott Stevens, Senior Vice President and General Counsel, Investment Company Institute, to Barry Barbash, Director, Division of Investment Management, Securities and Exchange Commission (May 20, 1996).

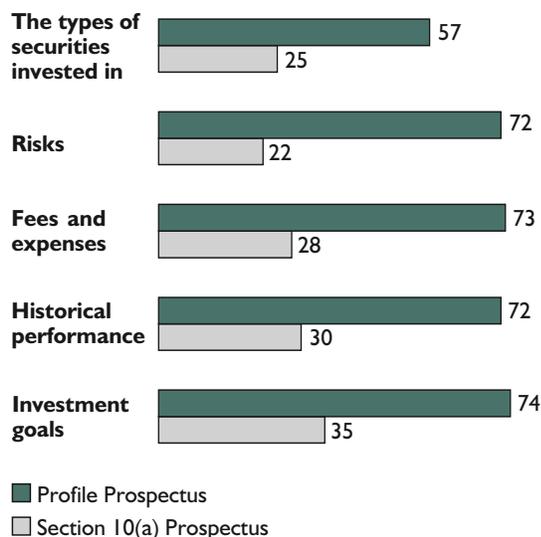
⁶ Previous Institute research found that a far smaller percentage of survey respondents—26 percent—indicated they had used the Section 10(a) prospectus as a source for mutual fund information. Whereas the current Institute research study is limited to recent purchasers, respondents to the earlier Institute study were broadly representative of all mutual fund shareholders. See *Piecing Together Shareholder Perceptions of Investment Risk* (Investment Company Institute, Spring 1993) at page 26.

Figure 1

Ease of Locating Selected Information in the Section 10(a) and Profile Prospectuses

(percent of recent buyers indicating very easy to locate)

Far more recent buyers found it very easy to locate important information in the profile prospectus.



Note: Number of respondents varies.

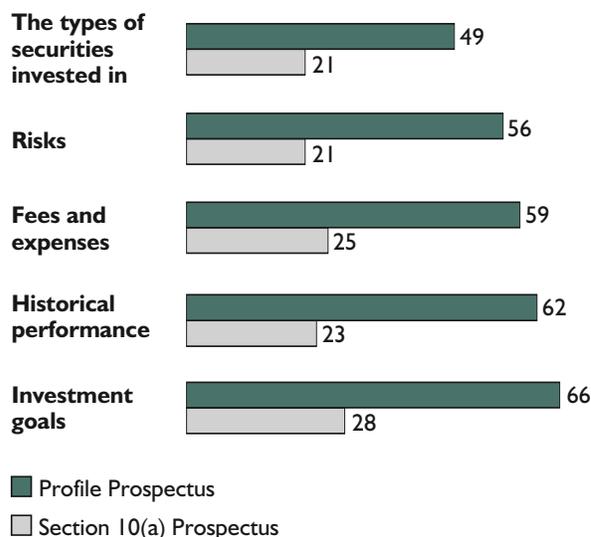
Source: The Profile Prospectus: An Assessment by Mutual Fund Shareholders, Volume I, Institute Research (Investment Company Institute, May 1996).

Figure 2

Ease of Understanding Selected Information in the Section 10(a) and Profile Prospectuses

(percent of recent buyers indicating very easy to understand)

Far more recent buyers found it very easy to understand important information in the profile prospectus.



Note: Number of respondents varies.

Source: The Profile Prospectus: An Assessment by Mutual Fund Shareholders, Volume I, Institute Research (Investment Company Institute, May 1996).

2. Mutual fund investors strongly favor the contents, format, and overall utility of the profile prospectus.

Investors believe the profile prospectus contains the right amount of information for making investment decisions. Seventy percent of the recent fund buyers surveyed by the Institute stated that the profile prospectus provided them with the right amount of information with which to make investment decisions (Figure 3). Moreover, the format of the profile prospectus appealed equally to those investors who had used the Section 10(a) prospectus in their most recent purchases and to those who had not, an indication that the profile prospectus would be used broadly by both groups if it were available.

Scudder's survey of prospective investors found more than 80 percent saying that the profile prospectus was just the right length and more than 85 percent

indicating that each of the 11 items in the profile prospectus was very useful in making an investment decision. Seventy-nine percent of respondents to Vanguard's survey of prospective investors rated the profile prospectus as excellent or good for providing sufficient information for making investment decisions.

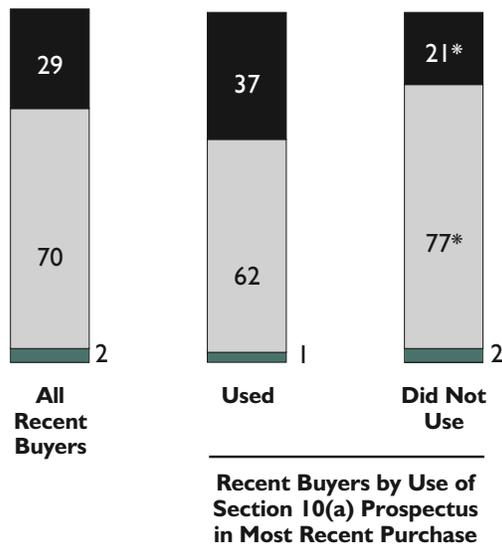
Investors can readily locate and easily understand information presented in the profile prospectus. A majority of the recent fund investors surveyed by the Institute said it was very easy to locate key investment items in the profile prospectus, and a majority said it was very easy to understand the discussions of these items. For example, 72 percent of respondents said it was very easy to locate information on fund risks in the profile prospectus, and 56 percent said it was very easy to understand the discussion. (Figures 1 and 2).

Figure 3

Assessment of the Amount of Information in the Profile Prospectus

(percent of recent buyers)

Most recent buyers—including those who had used the Section 10(a) prospectus—found that the profile prospectus had the right amount of information.



The profile prospectus had:

- Too little information
- Right amount of information
- Too much information

Number of Respondents

All Recent Buyers=998
 Used=484
 Did Not Use=514

*Prospectus users and nonusers are statistically different at the 95 percent level.

Source: *The Profile Prospectus: An Assessment by Mutual Fund Shareholders, Volume I, Institute Research (Investment Company Institute, May 1996).*

More than 90 percent of fund inquirers responding to Fidelity’s survey thought the profile prospectus’ discussions of fund performance, goals, and risks were useful. Also in Fidelity’s survey, more than three fifths of the prospective buyers thought the profile prospectus was better than the Section 10(a) prospectus for finding information and for presenting information clearly. In Scudder’s survey, more than 80 percent indicated that the profile prospectus was easy to read, was well-organized, and made it simple to focus on key issues about the fund.

- **Investors regard the profile prospectus to be more useful than the Section 10(a) prospectus for making investment decisions.** Nearly 60 percent of recent fund buyers surveyed by the Institute rated the overall usefulness of the profile prospectus higher than that of the Section 10(a) prospectus. Even the majority of those investors who used a Section 10(a) prospectus in their most recent purchases rated the profile prospectus higher (Figure 4). In addition, two thirds of all recent buyers would place the profile prospectus at or near the top of their

list of information sources. In contrast, 57 percent put the Section 10(a) prospectus at the middle or bottom of the list.

In Fidelity’s survey of prospective investors, more than half rated the profile prospectus as better than the Section 10(a) prospectus for making investment decisions. In Dreyfus’ survey of prospective investors, 49 percent said the profile prospectus was extremely useful for making fund investment decisions.

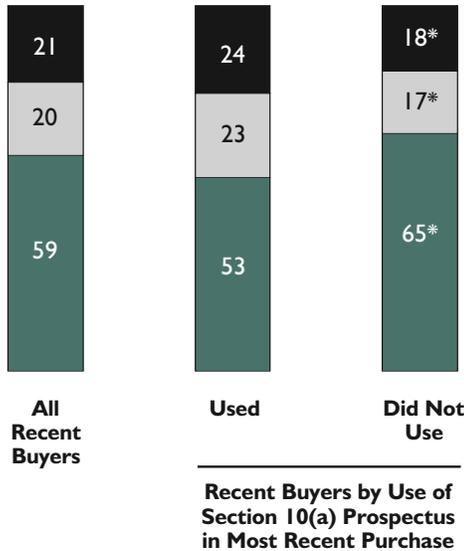
- **Professional financial advisers view the profile prospectus as assisting investors in their investment decisions.** In Capital Research’s survey of financial advisers, 87 percent preferred the profile prospectus over the Section 10(a) prospectus for helping investors make an investment decision. In addition, the majority of advisers responding to American Express’ survey gave higher marks to the layout, length, and content of the profile prospectus than to the Section 10(a) prospectus. For example, 56 percent of advisers rated the length of the profile prospectus as excellent, while only 10 percent of respondents gave the Section 10(a) prospectus this rating.

Figure 4

Overall Assessment of the Profile Prospectus Relative to the Section 10(a) Prospectus

(percent of recent buyers)

Most recent buyers—including those who had used the Section 10(a) prospectus—gave a higher evaluation to the profile prospectus.



Profile prospectus received:

- Lower evaluation than Section 10(a) prospectus
- Same evaluation as Section 10(a) prospectus
- Higher evaluation than Section 10(a) prospectus

Number of Respondents

All Recent Buyers=977
Used=476
Did Not Use=502

*Prospectus users and nonusers are statistically different at the 95 percent level.

Source: *The Profile Prospectus: An Assessment by Mutual Fund Shareholders, Volume I*, Institute Research (Investment Company Institute, May 1996).

3. The majority of investors who do not currently use the Section 10(a) prospectus would use the profile prospectus, if it were available.

- The Institute survey of recent fund buyers found that 61 percent of those who had not consulted a Section 10(a) prospectus for any purpose stated they would be very likely to use the profile prospectus, if it were available. Moreover, even among those who do use the Section 10(a) prospectus, 71 percent would be very likely to use the profile prospectus.

Research of the participating mutual fund companies also found that investors would use the profile prospectus. In Scudder’s survey of prospective investors, 64 percent found the profile prospectus to be very useful for making investment decisions. In Vanguard’s survey, 57 percent of prospective investors preferred the profile prospectus over the Section 10(a) prospectus for evaluating fund investments.

4. Mutual fund shareholders would prefer to be provided with the profile prospectus for investment decisionmaking.

- A substantial majority of mutual fund investors would like to receive the profile prospectus, provided the Section 10(a) prospectus would be available upon request. Two thirds of recent fund investors surveyed by the Institute indicated that, in making an investment decision, they would like to receive the profile prospectus by itself or with the option of obtaining a Section 10(a) prospectus from the fund company (Figure 5).

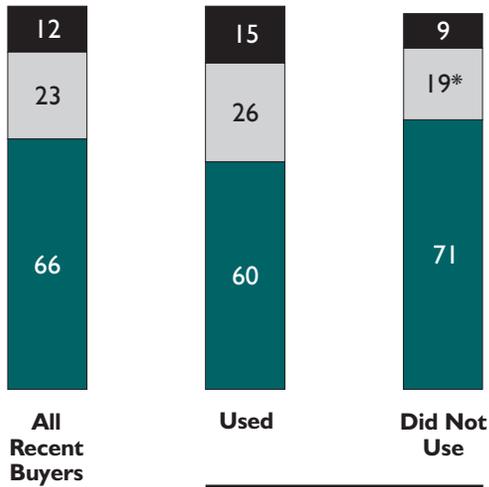
Institute members’ research also indicated that mutual fund investors would like the opportunity to use the profile prospectus in this fashion. For example, 62 percent of the shareholders in American Express’ survey would prefer to receive the profile prospectus, either alone or with the option of requesting a Section 10(a) prospectus.

Figure 5

Preference for Receiving the Section 10(a) and Profile Prospectuses

(percent of recent buyers)

Most recent buyers—including those who had used the Section 10(a) prospectus—preferred to receive the profile prospectus, either alone or with the option to receive the Section 10(a) prospectus upon request.



Recent Buyers by Use of Section 10(a) Prospectus in Most Recent Purchase

Preferred to receive:

- The Section 10(a) prospectus, either alone or with the option to receive the profile prospectus upon request
- Both the Section 10(a) and the profile prospectuses together
- The profile prospectus, either alone or with the option to receive the Section 10(a) prospectus upon request

Number of Respondents

All Recent Buyers=994
Used=480
Did Not Use=514

*Prospectus users and nonusers are statistically different at the 95 percent level.

Source: *The Profile Prospectus: An Assessment by Mutual Fund Shareholders, Volume I*, Institute Research (Investment Company Institute, May 1996).

Fidelity’s survey of fund inquirers found that 61 percent favored receiving the profile prospectus along with an 800 telephone number through which the Section 10(a) prospectus could be requested.

- **Professional financial advisers would use the profile prospectus with current and prospective customers.** In Capital Research’s survey of professional financial advisers, 78 percent said they were very likely or extremely likely to use the profile prospectus in face-to-face meetings with investors. In American Express’ adviser survey, 75 percent said that they would prefer to send investors the profile prospectus, either alone or with the option to request a Section 10(a) prospectus.

DEFINITIONS

Section 10(a) Prospectus

The “Section 10(a) prospectus” refers to the prospectus that funds currently deliver to shareholders pursuant to Section 10(a) of the Securities Act of 1933.

Profile Prospectus

The “profile prospectus” refers to the prototype prospectus developed at the initiative of the SEC to address investor needs for simple and more understandable disclosure when making investment decisions. It is limited to information on the II areas prescribed by the SEC.