

## Comment Letter on Proposed New Disclosure Option for Open-End Management Investment Companies, June 1997

June 9, 1997

Mr. Jonathan G. Katz  
Secretary  
Securities and Exchange Commission  
450 Fifth Street  
Stop 6-9  
Washington, D.C. 20549

**Re: Proposed New Disclosure Option for Open-End Management Investment Companies  
(S7-18-96)**

Dear Mr. Katz:

The Investment Company Institute<sup>1</sup> appreciates the opportunity to express its views on the Securities and Exchange Commission's proposed new rule that would permit mutual funds to provide investors with a fund "profile,"<sup>2</sup> a concise new disclosure document specifically designed by the Commission to convey information essential to an investment decision. The Commission's proposal recognizes the many benefits of such a document, as these have become apparent in the course of the Commission's almost two year old pilot program and related research on the profile.

The proposed amendments to Form N-1A<sup>3</sup> — together with the profile proposal, the proposed rule regarding fund names,<sup>4</sup> and the extended consideration given to improving risk disclosure — represent the most significant and comprehensive effort ever undertaken by the Commission to improve mutual fund disclosure. Launched by Commission Chairman Arthur Levitt, Jr. in 1994, this historic effort promises to redound to the lasting benefit of the more than 63 million investors who use mutual funds today. It is especially noteworthy that two fundamental considerations have guided the Commission's work from the inception of this project: first, that millions of fund investors clearly need and want the ability to use the profile; and second, that the profile can and should be authorized without loss of crucial investor protections.

The Institute highly commends Chairman Levitt, the Commission, and its staff on this initiative, and strongly supports the Commission's proposal to authorize fund profiles. Our comments and recommendations, as set forth below, are intended to further enhance the utility of the profile and encourage its widespread use by mutual funds as a supplement to their prospectuses.

### I. Background and General Comments

In October 1994, Chairman Levitt expressed concern about the length and complexity of mutual fund prospectuses and launched an innovative project to improve mutual fund disclosure.<sup>5</sup> A critical part of that initiative was asking mutual funds to create a "profile prospectus" that would summarize information essential to an investment decision and would complement the long-form prospectus. Chairman Levitt expressed his view that investors would benefit from a summary that would contain standard information in a standard format.

In response to Chairman Levitt's initiative, the Institute and eight mutual fund groups<sup>6</sup> in close consultation with the Commission staff and with the North American Securities Administrators Association, began work to develop a prototype of a profile. In August 1995, the Commission staff approved use of the prototype for a one-year trial period, and in July 1996 approved use of a revised profile and extended the pilot program for an additional year. Since the start of the pilot program, participating fund groups have developed profile prospectuses for 61 equity, bond, and money market funds and provided them to prospective investors.

During the pilot program, the Commission as well as the Institute and participating mutual funds undertook a variety of research to

determine investor needs and preferences concerning the format, contents, and style of mutual fund disclosure in the profiles as compared to the long-form prospectus.<sup>7</sup> The results of that research support Chairman Levitt's observation that "what investors request time and time again is a fund prospectus that they can read, in language they can understand, in a form they can follow."<sup>8</sup> The Commission's findings — and those of the Institute and its members — provide an exceptionally strong basis for the Commission to go forward in adopting the proposed profile rule.

Most importantly, by adopting the profile rule, the Commission would address the clear need for a fund disclosure document that many more of today's 63 million fund shareholders actually will read and use in making investment decisions. All of the research confirms that the profile will provide investors with the information they need to make an investment decision. For example, the vast majority of participants in the Institute's survey indicated that they would be very likely to use the profile to make investment decisions if it were available. This finding applied both to investors that were not inclined to use the long-form prospectus and those who were so inclined. Among those who had not used a long-form prospectus in their most recent purchases, 61 percent said they were very likely to read the profile. Thus, it would appear the profile would provide a very useful new source of information for those mutual fund buyers not inclined to use the long-form prospectus. An even higher percentage of those who had used the long-form prospectus (71 percent) reported that they were very likely to read the profile. This finding bears out the Commission's observation that the profile would provide investors with more options, rather than less information.

The reasons for this broad investor preference for the profile is clear. A substantial majority of the mutual fund shareholders surveyed by the Institute (70 percent) stated that the profile provides the right amount of information, and more than half of recent purchasers surveyed by the Institute found it very easy to understand the information in the profile prospectus on investment goals, investment risks, fees and expenses, how to redeem fund shares, and historical performance. Investors also gave high marks to the layout, organization, length and clarity of the profile prospectus. For example, in Scudder's survey, more than 80 percent of investors indicated that the profile prospectus is easy to read, clearly written, user-friendly, understandable, well-organized, and well-focused on key issues.<sup>9</sup> Vanguard found that 80 percent of investors gave the profile prospectus an overall evaluation of excellent or very good.<sup>10</sup>

Institute research showed that many investors would make the profile one of their top information sources.<sup>11</sup> The vast majority of investors surveyed by the Institute (66 percent) would like to receive the profile, either alone or with the option to receive the long-form prospectus. The research results reported by the participating mutual fund companies are consistent with the Institute's findings.<sup>12</sup>

Because the information required to be included in the profile is limited and its presentation is standardized, the profile also will permit investors to compare easily the attributes of several different funds. In fact, sixty percent of those surveyed by the Institute gave the profile a positive rating (of excellent or good) on its usefulness in making comparisons between or among funds. The proliferation of the number of funds in recent years makes it particularly important for the Commission to provide investors with the profile as a tool that can assist them in their comparison of this wide range of investment options. Investors currently have the option to choose from, for example, more than 825 different growth funds and over 325 government bond funds. The ability of investors to use the profile is also important in the context of the retirement plan market because it will provide these investors with the means to easily choose the particular funds, among many, that best suit their individual needs and preferences. Many retirement plans offer employees a wide variety of investment options, which can complicate the process of choosing a specific fund investment. The availability of the profile with which to compare investment options (as opposed to traditional prospectuses that are long and unwieldy for such purpose) would greatly help participants to make informed investment decisions.

It is most significant that the Commission proposes to provide the investing public with an important new disclosure tool without in any way compromising investor protection. Proposed Rule 498 would strictly regulate the content and format of the profile and would prohibit the inclusion of any extraneous information. A fund's long-form prospectus — itself subject to substantial improvements proposed separately by the Commission — would be readily available upon request as would the fund's shareholder reports. This fact would be prominently disclosed to investors through a legend in the profile inviting them to call a toll-free telephone number. The long-form prospectus, in any event, would be delivered not later than confirmation. In short, the profile would not reduce, but would expand, the information available to investors. The Commission staff would have the opportunity to review profiles before use to help assure that they comply with the requirements and are consistent with the fund's long-form prospectus.<sup>13</sup> Provisions of the federal securities laws would apply to assure the accuracy and completeness of the profile pursuant to such requirements.

In sum, a very compelling case exists for the Commission to adopt the proposed profile rule, and thereby permit investors, at their option, to use the profile for making fund purchases.

Our specific comments on the profile proposal follow.

## II. Format of the Profile

## A. Headings

Funds should have the flexibility to choose the type of heading for the prescribed disclosure topics — i.e., funds should be permitted to use either the proposed question format or narrative statements. Because the order of the headings would be identical for all funds and the substance of the headings would be substantially the same, this would not detract from the use of profiles to compare different funds.<sup>14</sup> Either alternative would appear to convey information to investors in an equally effective manner.

## B. Risk/Return Summary

The Commission indicated in the Release that, to the extent requirements for the risk/return summary change in response to comments or otherwise, conforming amendments would be made to both the profile rule and Form N-1A. We generally support this approach. Our comments on Form N-1A's proposed risk/return summary apply equally to the first four items of the profile, with one exception.<sup>15</sup> The Form N-1A letter recommends that a fund's statutory prospectus provide a means for obtaining additional information about the fund in one standardized, prominent location (namely, the prospectus's back cover page) rather than scattering this information throughout the prospectus.<sup>16</sup> While we believe that this is the most sensible approach for the Commission to follow with respect to the statutory prospectus, we believe that the Commission should take a different approach with respect to the profile by also requiring a fund profile to include in the discussion of a fund's main investment strategies a reference to the availability of the fund's shareholder reports and a means to obtain these reports.<sup>17</sup> Profiles containing this disclosure, along with the cover page disclosure providing a means for investors to obtain additional information about the fund, will unambiguously provide recipients of the profile with a convenient means to obtain additional information about the fund. These requirements taken together serve to underscore the profile's nature as a summary document and the ready availability of additional information about the fund.

## C. Multiple Fund Profiles

The Institute supports the Commission's proposal to permit a profile to contain information about more than one fund. This approach has the distinct advantage of providing potential investors with easily comparable information about several investment alternatives in one document.<sup>18</sup> For example, a fund complex could provide investors with a profile containing key information about each of the complex's equity funds. Similarly, a multiple fund profile could be used to describe all of the investment options available through a retirement plan.<sup>19</sup>

Whether or not the Commission permits multiple fund profiles, the Institute strongly recommends that the Commission permit multiple feeders of a single master fund and multiple classes of a multiple class fund to be presented in one profile. Most of the information in the profile would be identical for all of the feeders (or classes), including, for example, the fund's goals, the fund's investment strategies, the main risks of investing in the fund, and the fund's investment adviser. Differences among the feeders (and classes), which would include fees charged, performance (because of the difference in fees), and the method of purchasing the particular feeder's shares, could be explained easily in a single profile. The costs associated with requiring funds to produce a different profile for each feeder (or class) would not be warranted under these circumstances.<sup>20</sup>

# III. Contents of the Profile

## A. Cover Page

Under the Commission's proposal, funds would include the following information on the cover page of the profile (or at the beginning of the profile if the profile is distributed electronically or as part of another document): the fund's name, and, at its option, the fund's investment objectives or the type of fund offered or both; the approximate date of the profile's first use and, if applicable, the date of the fund's most recent performance information included in the profile; a statement identifying the document as a profile; and a specific legend.

The Commission should revise the proposed requirements in two respects. First, any fund profile, regardless of the manner of its distribution, should be permitted to provide the basic identifying information described above either on the cover page or at the beginning of the profile. The Release does not suggest, and we do not believe there is, any reason to require fund profiles to have a separate cover page. Requiring a separate cover page would add to fund profile printing costs without any apparent offsetting benefit to investors (who would be provided with the same basic identifying information about the fund at the beginning of the profile). Second, funds should not be required to include the date of the fund's most recent performance information on the cover page or at the beginning of the profile. Providing two different dates, whether on the cover or in close proximity at the beginning of the profile, might confuse investors. Instead, the date of the most recent fund performance should be provided alongside that performance, which likely would appear later in the body of the profile pursuant to Rule 498(c)(2)(iii) (either as part of a reprinted profile or on a separate "stamp" or "sticker" that reflects the updated performance).

The legend about the availability of additional information on the fund (including the availability of the fund's long-form prospectus)

should be required to appear either on the cover page or at the beginning of the profile. Inserting the legend up front should help make it clear that investors may obtain the fund's long-form prospectus and other information about the fund before making an investment decision. We recommend, however, that the Commission modify Rule 498 to permit such additional information about the fund to be obtained from financial intermediaries (in addition to, or instead of, permitting investors to obtain this information from the fund itself).<sup>21</sup> Funds commonly enter into agreements with broker-dealers or banks that sell fund shares to provide requesting investors with information about the fund. There is no reason to permit only the fund (and not these intermediaries) to send the requested information to investors. Such a requirement would unnecessarily disrupt current fund operations without any corresponding benefit to fund shareholders.

The Commission requested comment on two possible formulations of the legend notifying investors of the availability of additional information about a fund. We urge that the Commission adopt the legend proposed as an alternative in the Release, with one important modification. The alternative legend would better inform investors of the profile's nature as a summary document and the availability of a fuller description about the fund in the fund's long-form prospectus. We are concerned, however, that, as proposed, the legend would refer investors to additional "material" information about the fund. Information contained in the long-form prospectus indeed may be "material" for various purposes. Nonetheless, the proposed legend would so characterize information that is omitted from the profile in keeping with its character as a summary disclosure document, and thus would imply that the profile is legally deficient even where the contents of the profile strictly comply with the Commission's own detailed rules. To avoid this erroneous implication, we recommend that the legend read as follows:

This Profile summarizes key information about the Fund that is included in the Fund's prospectus. The prospectus includes additional information about the Fund that you may want to consider before you invest. You may obtain the Fund's prospectus and other information about the Fund (by calling \_\_\_\_\_) (or) (by contacting your broker or financial adviser.)

The Institute also recommends that the Commission give funds the flexibility to call this document a "profile" or a "profile prospectus." The Release does not contain any justification for imposing any restriction on a fund's use of the term, "profile prospectus." Clearly, the term is appropriate and accurate because the profile is a prospectus under the federal securities laws. In view of this legal status and its attendant consequences, prohibiting funds from calling this document a profile prospectus seems unreasonable.<sup>22</sup>

## **B. Portfolio Manager Disclosure**

The Institute generally supports the proposed approach regarding disclosure of investment advisers, subadvisers, and portfolio managers. The proposal would require a fund to identify its investment adviser and portfolio manager and to disclose the length of time that the portfolio manager has managed the fund and his or her business experience for the last five years. Recognizing that a fund may have more than one portfolio manager, proposed Rule 498 would require the name and the last five years of business experience for any portfolio manager who "manages 40% or more of the Fund's portfolio."<sup>23</sup> The Commission should make two technical clarifying changes to this standard. First, Rule 498(c)(2)(v) should be modified to apply the 40% standard to "the net assets of the fund's portfolio" rather than "the fund's portfolio." This would provide funds with more guidance regarding the appropriate measurement to make in determining whether disclosure about a particular portfolio manager is required. Second, the rule should require disclosure about any portfolio manager that is "reasonably expected to manage," rather than "manages," 40% or more of the fund's net assets. This formulation would take into account changes in the amount of the fund's net assets over time that may alter the percentage of its net assets managed by a particular portfolio manager.

## **C. Purchases and Redemptions of Fund Shares**

Proposed rule 498(c)(2)(vi) would require a fund to provide information about how to purchase a fund's shares, including any minimum investment requirements<sup>24</sup> and to disclose any breakpoints in, or waivers of, sales loads. The Release notes that, apart from the general requirement to provide summary information and concise disclosure, Rule 498 would not limit the extent of purchase information in a profile and specifically invites comments as to whether limitations are warranted.

The Institute strongly recommends that the Commission specifically limit the amount of purchase information that funds are required to provide in the profile. More specifically, the Commission should only require funds to identify the existence of breakpoints in sales loads and the existence of those waivers that would be required to be disclosed in the fund's prospectus.<sup>25</sup> Many funds have extensive variations in sales loads and a variety of circumstances under which sales loads may be waived. Disclosure of all these variations and circumstances would be lengthy and at odds with the profile's intended purpose as a summary disclosure document. Investors already would be informed of a fund's maximum sales load through the profile's fee table. Further, under the Conduct Rules of the National Association of Securities Dealers, broker-dealers must disclose sales charges in recommending the purchase of a mutual fund.<sup>26</sup>

Proposed Rule 498(c)(2)(vii) would require funds to provide information about how to redeem the fund's shares and would not specifically limit the extent of information required (other than through the general requirement that funds provide summary and concise information). Consistent with our views regarding the proposed purchase information, the Institute strongly recommends that

the Commission revise this instruction to specifically require funds to state that the fund's shares are redeemable, to identify the procedures for redeeming shares (e.g., on any business day by written request, telephone or wire transfer), to identify the existence of any charges or sales loads that may be assessed upon redemption, and to identify the existence of waivers of these charges to the extent that information about these waivers would be required to be disclosed in the fund's prospectus.<sup>27</sup>

In addition to providing more specific instructions regarding purchases and redemptions, Rule 498 should permit the purchase and redemption portions of the profile to include a phone number that investors may use to obtain further information. This approach would provide investors with summary information about purchases and redemptions in the profile while also providing a convenient means to obtain additional information promptly.

## D. Other Services Available

The Commission should revise the instruction regarding available fund services to make clear that a fund would not be required to disclose all available services. Such a requirement would produce lengthy but not particularly useful disclosures of a sort inconsistent with the summary character of the profile. Funds should have the flexibility to disclose those services that they believe are appropriate for inclusion in a profile.

## E. Purchase Applications

Proposed rule 498(b) provides that "[a] Fund may provide a Profile to investors, which may contain an application that investors may use to purchase the Fund's shares . . ." (emphasis added). The quoted rule text suggests that a purchase application would be required to be physically part of any fund profile. We do not believe there is any reason for such a requirement and ask that the Commission make clear that a fund may design a profile so that it does not physically contain, but instead is accompanied by, a purchase application (in addition to being permitted to include a purchase application as part of the profile).

# IV. Filing Requirements

The Commission should require a profile to be filed with the Commission at least 30 days in advance of use in two circumstances — before its first use and when a fund has been added to an existing profile.<sup>28</sup> We believe that it is important for the Commission staff to monitor compliance with Rule 498's disclosure requirements. For example, the first four items of the profile and the risk/return summary in Form N-1A would contain substantially similar disclosure and staff review of and comments on this disclosure should be done in a consistent manner. Staff review should help assure that profiles maintain a high quality of disclosure in keeping with the Commission's regulatory objectives. It is essential for the staff to be mindful of not making comments, like those made in the past on fund prospectuses, that will result in "disclosure creep".<sup>29</sup> Rather, the staff should conscientiously provide comments that advance the Commission's goal of maintaining the fund profile as a summary and concise disclosure document.

The Commission has proposed that funds be required to file any profile that contains substantive changes to a previously filed profile 30 days before use. We recommend instead that such a profile (other than one that adds a new fund) be required to be filed with the Commission no later than the fifth business day after the date it is used. To require pre-use filing with the Commission for any substantive change would be burdensome and unnecessary. For example, under the Commission's proposed filing requirement, a fund that added a new purchase option or eliminated an account maintenance fee would be required to file a profile reflecting these changes with the Commission at least 30 days before using that profile.

## V. Delivery of Additional Disclosure Documents

Proposed Rule 498(b)(2) would require a fund to send its prospectus, statement of additional information, and shareholder reports within 3 business days of a request. Consistent with our recommendations on proposed Form N-1A, we recommend that the Commission instead adopt a standard requiring that, upon request, these documents be sent "reasonably promptly," which normally would be deemed to be within 3 business days. This standard would provide necessary flexibility for unforeseen circumstances that are beyond a fund's control (such as disruptions caused by severely inclement weather, prolonged power outages, or occasional, minor operational delays).<sup>30</sup>

The Institute also urges the Commission to make it clear that funds are not required to keep detailed records of the date of each and every request for these disclosure documents, but rather should adopt procedures designed to test periodically compliance with the "reasonably promptly/normally 3 business day" standard. We believe that such a clarification is necessary in light of certain statements in the Release regarding the Commission staff's plans to examine for compliance with the 3 business day requirement and the Commission's intention to bring an enforcement action in an appropriate case for failing to comply with this requirement.<sup>31</sup>

# VI. Profiles Tailored for Retirement Plan Participants

The Commission sought comment regarding use of the profile in the retirement market and, in particular, its usefulness to investors



who purchase mutual funds through their participant-directed defined contribution plans. The Institute believes that the profile could be extremely helpful to such investors for evaluating and comparing the funds offered to them as investment alternatives in a retirement plan. Because these investors are a significant and growing percentage of today's mutual fund shareholders,<sup>32</sup> it is important that mutual funds be permitted to provide appropriate, meaningful disclosure that is designed specifically to meet their needs.

Certain information otherwise required to appear in the profile would not be applicable to retirement plan participants. The Commission should, therefore, permit funds to adapt the profile for the retirement plan investor and, in particular, to omit irrelevant information, as explained below.

## **A. Omission of Information Not Relevant to Retirement Plan Participants**

The Commission proposes to permit a profile that would be used in connection with certain retirement plans to omit purchase information, redemption information, distribution and taxation information, and information regarding fund services that would be required in profiles used outside of the retirement market. The Institute supports this aspect of the proposal. The purchase and redemption information that would be required to appear in profiles used outside of the retirement market is not applicable to plan participants, who buy and sell shares through procedures established by their respective retirement plans. Nor is the distribution and taxation information that would be required in profiles used outside of the retirement market relevant to retirement plan participants, to whom a different distribution and tax regime applies. Similarly, information that would be required regarding exchange privileges and other services may not be relevant to investors purchasing shares in a retirement plan.

Information regarding retirement plan eligibility, participant enrollment and the plan's purchase and sale procedures is provided by the plan sponsor, typically the employer. Likewise, information regarding a plan distribution and its tax consequences, the exchange of one investment option for another and other plan services should be provided by the plan sponsor. Both the Employee Retirement Income Security Act of 1974 ("ERISA") and the Internal Revenue Code impose legal obligations on plan sponsors with respect to providing such information. For instance, under the reporting and disclosure requirements of ERISA, plan fiduciaries disclose plan-specific information regarding enrollment, eligibility and plan procedures to all plan participants in a summary plan description.<sup>33</sup> Moreover, plan distribution and related tax information is required to be provided to participants prior to the distribution of assets from a plan.<sup>34</sup>

The Institute supports the Commission's proposal insofar as it would permit funds, at their election, to adapt the profile by omitting information of this kind from any profile provided to only retirement plan investors. Furthermore, because the plan sponsor generally is obligated to provide the relevant analogous information to these individuals, the Commission should not require the addition of any information to replace that which is omitted. In fact, because many details, such as those regarding transfers between investment options and specific plan services, will differ from plan to plan, it would be impractical to require a fund's profile to include such information.

Nonetheless, the Commission should provide flexibility for funds that desire to include such information in a profile expressly designed for the retirement market. Specifically, funds should be permitted either to include in the profile information regarding retirement plan purchases and sales, the taxation of plan distributions and the transfer of participant account assets among investment options, or to describe a source from which this information may be obtained. For example, a fund may wish to omit tax information relevant to retail investors, and instead include a statement that plan distributions are generally taxable as ordinary income, but income averaging rules may apply, and that further details may be obtained from the plan sponsor.

The Commission also should permit funds to tailor the profile as suggested for any defined contribution plan even if it does not meet the requirements for qualification under the Internal Revenue Code. Participants in any defined contribution plan have the responsibility for making investment decisions, and the Commission should not distinguish among them in permitting funds to tailor profiles to meet their information needs.

## **B. Distinguishing Legend For Retirement Plan Profile**

Adapting the profile for the retirement markets, as described above, would result in the omission of certain information that otherwise must be included in the retail profile. It also may result in the inclusion of additional information relevant only to retirement plan participants. For this reason, we recommend that any such version of the profile carry a clear legend stating that it is intended only for retirement plan participants and not suitable for use by other investors.

## **VII. Unit Investment Trust Profiles**

The Institute commends the Commission on its willingness to consider permitting unit investment trusts, or UITs, to use a profile. No less than mutual fund investors, investors in UITs would benefit from the opportunity to receive and make an investment decision based on a profile. The Institute plans to submit detailed recommendations to the Commission regarding such a UIT profile as soon

as possible following the adoption of a mutual fund profile rule.

## VIII. Effective Date

Neither the Release nor the profile rules provide an effective date for use of fund profiles. Because the first four items of the profile would be substantially identical to the disclosure required in the proposed risk/return summary at the beginning of fund prospectuses, we expect that most fund groups will revise their long-form prospectuses and develop (or revise existing) profiles concurrently. The Institute requests therefore that the Commission permit funds to comply with the profile rules within the time period provided for compliance with the Form N-1A amendments.<sup>35</sup> The suggested approach would permit funds that have prepared profiles in accordance with current requirements to continue to use those profiles until they revise their long-form prospectuses and profiles to conform to any new rules.<sup>36</sup>

## IX. Disclosure Safeguards

As the Commission's Release makes clear, the profile is intended to serve vitally important policy objectives: to provide investors all the disclosures about a fund that are key to an investment decision, in a concise and easily-understandable document that more investors are likely to actually use, organized in a manner that will help them more readily compare the fund choices available to them. These objectives will become all the more compelling with continued growth in the number of mutual fund investors and the number of funds available to them. Clearly, there is every reason to encourage the wide development and use of fund profiles in order to more effectively inform fund investors, whether they are investing in a normal retail setting or as participants in a retirement plan.

As the Release also makes plain, the Commission intends to achieve this objective without compromising the rigorous standards of accountability that the federal securities laws impose on issuers of securities. The profile would be considered a summary prospectus under Section 10(b) of the Securities Act of 1933. As is the case for all Section 10 prospectuses, funds could be subject to liability for a misrepresentation of material fact in a profile or an omission of a material fact necessary in order to make the statements in the profile not misleading under Section 12(a)(2) of the Securities Act, Section 10(b) of the Securities Exchange Act of 1934, and Rule 10b-5 under the Exchange Act.

Nonetheless, because the profile is a summary prospectus that an investor may opt to use in purchasing fund shares, it raises novel regulatory and legal issues. First, are the contents of the profile appropriate? We strongly believe they are. The proposal reflects the extensive consideration the Commission has given to the feasibility of crafting regulations that would produce a summary prospectus appropriate for use at an investor's option — i.e., that would assure that a profile, if properly prepared by a fund, includes all the items of information essential for investment decisionmaking. As we have discussed, the profile has been subject to extensive empirical evaluation with this in mind. The Institute believes that the form of profile proposed by the Commission is wholly appropriate for this purpose, and its rule and instructions, faithfully implemented, would assure disclosure of all those items of information that are key to making an investment decision. The Commission's decision not to permit a fund to incorporate by reference its long-form prospectus into the profile appears to reflect the Commission's own judgment that the profile is not deficient in the items it covers.<sup>37</sup>

Second, what is the appropriate relationship between the profile and the long-form prospectus? We believe this relationship is apparent in the Commission's proposal, but it also should be made very clear in any final rule, instructions and release. In circumstances where a fund has prepared both its profile and its long-form prospectus in scrupulous compliance with the Commission's rules, the Institute is concerned that the fund nonetheless may be subject to plaintiffs' actions brought on behalf of investors who knowingly opted to use the profile to purchase fund shares (and thus to receive the long-form prospectus no later than the confirmation of purchase), solely on the basis that the profile (in keeping with its character as a summary disclosure document) omits certain information that is contained in the prospectus (consistent with the longer and more detailed disclosure it provides). Liability under such circumstances would undercut altogether the Commission's important innovation of the profile as a summary prospectus for mutual funds, with the result that no fund would be likely to avail itself of the authority granted under proposed Rule 498. The profile literally would become "a minefield" in which only the foolhardy would venture.<sup>38</sup>

In order to avoid such technical legal pitfalls, we would urge the Commission in an adopting release, instructions and rule to make its intent clear in certain specific respects. Under Section 12(a)(2) of the Securities Act, the adequacy of a fund profile will turn on whether it omits a material fact necessary in order to make the disclosures included in the profile, in light of the circumstances under which they were made, not misleading. The clarifications we seek are intended to assist a court in clearly understanding "the circumstances under which" the statements in the profile are being made. We specifically recommend that the Commission first, emphasize the summary nature of the profile; second, revise its position that the form of profile prescribed in its rules may be inadequate in certain unspecified circumstances; and third, affirm that a fund that complies in good faith with the Commission's requirements regarding the preparation and distribution of a profile should be able to rely on Section 19(a) of the Securities Act to defend against litigation that alleges that the fund omitted material information from the profile. Each of these points is discussed

below.

## 1. Emphasize the Profile's Characteristics

The Commission should reiterate the summary nature of the profile as providing a concise presentation of key information about a fund in a standard format. The Commission also should emphasize the highly prescriptive nature of its profile rule, which limits the profile to nine key items of information and provides specific instructions for each of the items.<sup>39</sup> In addition, the Commission should emphasize that the profile will supplement, not supplant, the long-form prospectus, and thus will only increase the total mix of information provided to investors about a fund.

The Commission also should take note that the profile has been purposefully designed to "bespeak summary": as proposed, it would clearly convey to investors that it provides a summary of key items of information about a fund, that the long-form prospectus and shareholder reports contain additional information, and that such information is readily and promptly available upon request. The Release does not address whether funds may, or should, request or obtain an acknowledgment from investors who purchase shares on the basis of a profile that they understand that additional information regarding the fund is available in the fund's long-form prospectus. The Commission should make clear that, at their option, funds may seek such acknowledgments, as a means of underscoring the summary character of the profile.

Finally, the Commission should clarify statements in the Release that tend to obscure the distinction between a profile and a prospectus — for example, by describing the Form N-1A amendments as focusing prospectus disclosure on essential information about a particular fund.<sup>40</sup> It is apparent that these statements were intended simply to emphasize the importance of the Commission's initiative to improve and simplify the Form N-1A disclosures. Nonetheless, such characterization may have the unanticipated effect of blurring the distinction between a profile and a long-form prospectus.

## 2. Clarify the Adequacy of the Profile's Contents

The proposed contents of the profile are the product of extensive Commission deliberation and research with investors about the categories of information that are necessary to making an informed investment decision. In the Release, however, the Commission states that "a fund would not be able to use a profile when material information relating to its particular circumstances is not addressed by the instructions for the 9 items of required disclosure." This plainly suggests that there are or may be categories of information not embraced by the Commission's rule that funds must (in circumstances unspecified) include in the profile. The Institute urges that the Commission revise this position in an adopting release. The Commission's statement could be read to indicate that a fund profile, faithfully incorporating all the nine items of information prescribed by the Commission, nonetheless may be deficient (and the fund therefore open to significant liability) because it omits some other item not identified in the Commission's rule. Such a result would be unfair and is at odds with the underlying premise of the proposal — that it is possible to design a prototype document that will provide information sufficient for an investment decision, albeit in summary form. We believe that the Commission's proposal succeeds in its objective of specifying all the items of information about a fund that are key to investment decisionmaking. Further, the Commission has gone to great lengths to ensure that investors understand that the profile does not contain all of the information about a fund and that more information about a fund can be easily obtained.

If the Commission believes, however, that there are additional information items that should be included, where applicable, its rule should specify them.<sup>41</sup> If funds are left simply to hazard a guess about "when material information relating to its particular circumstances is not addressed by instructions for the nine items" of disclosure included in the rule, they may be far less inclined to design and use profiles under any circumstances.

## 3. Clarify the Applicability of Section 19(a) of the Securities Act

No fund that conscientiously follows the Commission's rules should be held liable for omitting information in the profile that appears in its long-form prospectus. To affirm this principle, the Commission should prominently state in its adopting release on the fund profile rule that a fund that complies in good faith with the Commission's instructions in the preparation and distribution of a profile should be able to rely on Section 19(a) of the Securities Act to defend against litigation that alleges that the fund omitted material information from a profile.<sup>42</sup> There is ample precedent for the Commission to provide such assurances in the context of mutual fund disclosure. The Commission did so when it initially proposed Form N-1A. At that time, it took note of funds' concern that omitting information from the prospectus, and disclosing it in the SAI, would expose them to liability for the use of a prospectus that fails to state a material fact.<sup>43</sup> In the proposing release for Form N-1A, the Commission stated that:

the Commission believes in light of Section 19(a) that, under ordinary circumstances, the registrant's discussion of the various disclosure items of Form N-1A (as designated in Parts A and B) "in good faith in conformity with" the form would not result in liability under Section 12(2) . . . .<sup>44</sup>

Both the release adopting Form N-1A and the most recent release proposing amendments to Form N-1A restate the availability of



Section 19(a) to funds acting in good faith in conformity with Form N-1A.<sup>45</sup> The absence of such a statement in connection with the profile rules, in light of the statements accompanying Form N-1A, might give rise to the inference that Section 19(a) would not be available to defend a fund's use of the profile. The Commission should confirm that Section 19(a) would apply equally to funds acting in good faith in conformity with its profile rule.

In sum, it is likely that significantly more funds would develop profiles and more promptly make them available to investors if the Commission provided the clarifications outlined above in its adopting release and final rule and instructions on the profile: First, by emphasizing the summary nature of the profile; second, by revising its position that the form of profile its rules prescribe may be inadequate in certain unspecified circumstances; and third, by affirmatively stating that a fund that complies in good faith with the Commission's instructions in the preparation and distribution of a profile should be able to rely on Section 19(a) to defend against litigation that alleges that the fund omitted material information from the profile.

\* \* \*

## Conclusion

Mutual fund disclosure requirements administered by the Commission are a matter of vital importance to the millions of investors who use mutual funds to meet their retirement and other major financial needs. Under Chairman Levitt, the Commission has devoted exhaustive attention to addressing the needs of fund investors, and it has proposed disclosure reforms and innovations (including the profile) that would be of exceptional benefit to them. We respectfully urge the Commission to act expeditiously in adopting final rules in this area, including the proposed profile rule, to make it possible for mutual fund investors to receive a clear and concise disclosure document to assist them in making their investment choices. We appreciate the Commission's consideration of our comments. If you have any questions concerning our comments, please do not hesitate to contact me at 202/326-5810, Craig Tyle at 202/326-5815 or Dorothy Donohue at 202/326-5821.

Sincerely,

Paul Schott Stevens  
Senior Vice President  
General Counsel

cc: The Honorable Arthur Levitt, Chairman  
The Honorable Steven M. H. Wallman, Commissioner  
The Honorable Isaac C. Hunt, Jr., Commissioner  
The Honorable Norman S. Johnson, Commissioner  
Barry P. Barbash, Director, Division of Investment Management

### Appendix A

Rule 498(c)(1)(iv) would be revised to read as follows:

(iv) The following legend, which may be modified as described below:

This Profile summarizes key information about the Fund that is included in the Fund's prospectus. The prospectus includes additional information about the Fund that you may want to consider before you invest. You may obtain the Fund's prospectus and other information about the Fund (by calling \_\_\_\_\_) (or) (by contacting your broker or financial adviser).

Provide a toll-free (or collect) telephone number that investors can use to obtain the prospectus or other information and/or indicate (as appropriate) that investors can obtain this information by contacting their broker or financial adviser. The Fund may tailor this legend to refer to other financial intermediaries through which its shares are available (e.g., banks). If applicable, the Fund may indicate that the prospectus is available on its Internet site or by E-mail request.

### ENDNOTES

<sup>1</sup> The Investment Company Institute is the national association of the American investment company industry. Its membership includes 6,456 open-end investment companies ("mutual funds"), 440 closed-end investment companies, and 10 sponsors of unit investment trusts. Its mutual fund members have assets of about \$3,677 trillion, accounting for approximately 95% of total industry assets, and have over 59 million individual shareholders.

<sup>2</sup> SEC Release No. IC-22529 (February 27, 1997) ("Release").

<sup>3</sup> SEC Release No. IC-22528 (February 27, 1997) ("Form N-1A Release").

<sup>4</sup> SEC Release No. IC-22530 (February 27, 1997).

<sup>5</sup> See "Taking the Mystery Out of the Marketplace: The SEC's Consumer Education Campaign," Remarks by Arthur Levitt, Chairman, Securities and Exchange Commission before the National Press Club (October 13, 1994).

<sup>6</sup> American Express Financial Corporation; Bank of America N.T. & S.A.; Capital Research and Management Company; The Dreyfus Corporation; FMR Corp.; Scudder, Stevens & Clark, Inc.; T. Rowe Price Associates, Inc.; and The Vanguard Group, Inc.

<sup>7</sup> See, e.g., "The Profile Prospectus: An Assessment By Mutual Fund Shareholders," Report to the US Securities and Exchange Commission by the Investment Company Institute (May 1996) ("Profile Assessment"). The Institute's research was performed by an independent consultant, Response Analysis Corporation, of Princeton, New Jersey. Between November 1995 and March 1996, RAC conducted in-person interviews with 1,004 randomly-selected US investor households that had purchased at least one mutual fund in the previous five years. The survey respondents had demographic characteristics similar to mutual fund shareholders nationwide. Mutual fund complexes participating in the profile engaged in quantitative research concerning how their customers and, in some cases, investment advisers, brokers, and other financial professionals, assessed the effectiveness and usefulness of the profile prospectus. The approaches taken by the fund complexes varied considerably. Some conducted surveys of randomly selected prospective investors who had been sent a profile prospectus along with a long-form prospectus, while others included a control group that received the long-form prospectus but not the profile prospectus.

<sup>8</sup> Yip, Pamela, "SEC Seeks to Make Prospectuses Easier to Read," The Houston Chronicle, August 14, 1995 at 1, quoting remarks by Chairman Arthur Levitt at Press Conference to Announce the Distribution to Investors of the "Profile Prospectus" (July 31, 1995).

<sup>9</sup> Profile Assessment at 91.

<sup>10</sup> Id. at 102.

<sup>11</sup> Sixty-five percent of those who had consulted a long-form prospectus and 67 percent of those who had not done so said they would place the profile at or near the top of their lists of information sources.

<sup>12</sup> Dreyfus found that 49 percent of those surveyed who received the profile said it was very useful for making investment decisions. Profile Assessment at 44. In American Express's survey of current shareholders, 62 percent preferred to receive the profile prospectus, either alone or with the option of requesting a long-form prospectus. Id. at 10. In Fidelity's survey, 61 percent of respondents favored receiving the profile prospectus with a toll-free number through which they could order the long-form prospectus. Id. at 81.

<sup>13</sup> One commenter has argued that adoption of the profile rule would detract from efforts to make the long-form prospectus a readable document. The Institute strongly disagrees. Many fund complexes voluntarily have revised their long-form prospectuses to make them more readable and useful to investors. This trend continues, as it has throughout the time of the pilot project on the profile prospectus. Adoption of the Commission's proposed amendments to Form N-1A and the proposed application of plain English requirements to the risk/return summary of fund prospectuses will accelerate this process and further enhance the readability of fund prospectuses. The Institute's position is clear — the profile is not intended to substitute for the long-form prospectus, but instead to complement it. Numerous other commenters, equally concerned about the quality of disclosure to investors, have expressed strong support for the profile. See e.g., Norman G. Fosback, Profiles - A Valuable Tool for Investors, Mutual Funds (May 1997) ("[t]he most significant development, however, is implementation of fund profiles - a kinder, simpler, user-friendly alternative to today's cumbersome, legalistic, verbose fund prospectuses"); Timothy Middleton, Prospectusphobia, Mutual Funds (June 1997) ("[p]rofiles are designed to provide investors with all the information about a fund they need in order to decide whether they want to buy it").

<sup>14</sup> For the same reasons, the Institute strongly supports the Commission's proposal to permit funds to substitute substantially similar questions to those included in proposed Rule 498.

<sup>15</sup> See Letter from Paul Schott Stevens, Senior Vice President and General Counsel, Investment Company Institute to Jonathan G. Katz, Secretary, Securities and Exchange Commission (June 9, 1997) ("Form N-1A Letter").

<sup>16</sup> Id.

<sup>17</sup> The recommended disclosure for the profile would read as follows: "Provide disclosure to the following effect: Additional information about the Fund's investments is available in the Fund's annual and semi-annual reports to shareholders. In particular, the Fund's annual report discusses the relevant market conditions and investment strategies used by the Fund's investment adviser that materially affected the Fund's performance during the last fiscal year. You may obtain these reports at no cost (by calling \_\_\_\_\_) (or) (by contacting your broker or financial adviser). See *infra* at p. 7 for our recommendations regarding references to brokers and other financial intermediaries. The Commission should provide an exclusion from the requirement to disclose the

availability of annual and semi-annual reports for new funds that do not yet have such reports.

<sup>18</sup> The Commission should clarify that funds that use multiple fund profiles are permitted to present information that is common for all the funds in the profile only once. In other words, they should not have to repeat this common information (e.g., purchase and redemption information and information regarding fund services) for each of the funds in the profile. It appears that the Commission contemplated this result by referencing in the Release General Instruction C of the proposed amendments to Form N-1A "for guidance on disclosing information for more than one fund in the same prospectus." See Release at note 26. General Instruction C to the proposed amendments to Form N-1A provides that "[f]unds may group the response to any Item in any manner that organizes this information into readable and comprehensible segments . . ." We are seeking this clarification because Rule 498(c)(2), by mandating that the information required by Rule 498(c)(2)(i) through (ix) be provided in "the order indicated", suggests that funds would not have this flexibility.

<sup>19</sup> See *infra* at pp. 12-14 for additional comments regarding use of the profile in the retirement market. The Institute strongly believes that the profile has particular advantages even if it is limited to presenting information about a single fund. While our support for the profile is not dependent on the Commission authorizing multiple fund profiles, such authorization would encourage wider use of the profiles in circumstances clearly advantageous to investors.

<sup>20</sup> If the Commission ultimately decides not to generally permit the use of multiple fund profiles, the Institute recommends that the Commission modify the definition of fund in Rule 498(a)(1) to accommodate the presentation of multiple feeders of a single master fund in a single profile. The proposed definition of "fund" would not necessarily include all of the feeders in a master fund because feeders may be registered on separate registration statements. While it appears that under the proposed definition of fund in Rule 498(a)(1), several classes of a single fund would be permitted to be included in a single profile, to avoid any confusion, the Institute requests that the Commission make this clear in the adopting release.

<sup>21</sup> See note 30, *infra*, for our specific suggestions on how Rule 498(b)(2) should be revised to implement these recommendations. Attached as Appendix A is a revised Rule 498(c)(1)(iv) that reflects this recommendation as well as our other recommended changes to the proposed legend.

<sup>22</sup> A profile likely would be sent to prospective investors with a cover letter, which would be considered to be a Rule 482 "omitting prospectus." (A profile may not be accompanied by supplemental sales literature under the federal securities laws, unless it also accompanied or preceded by a Section 10(a) prospectus. See, e.g., Release at note 92.) Rule 482(a)(3) requires an omitting prospectus to state conspicuously "from whom a prospectus containing more complete information may be obtained and that an investor should read that prospectus carefully before investing . . ." Such a statement in a cover letter (or other omitting prospectus) accompanying a profile (which would include a purchase application) would be very confusing. It would not be clear to the recipients of these materials whether they could invest in the fund based on the profile or whether they first would be required to obtain the long-form prospectus. Therefore, the Commission should interpret Rule 482 to permit the profile to suffice for these purposes and to permit funds to tailor the legend accordingly. The Commission also should make clear that funds that accompany a profile with an omitting prospectus would not be violating Rule 482(a)(5)'s requirement that an omitting prospectus not be "accompanied by any application by which a prospective investor may invest in the investment company. . . ." This requirement is intended to prohibit an omitting prospectus from being used as a selling document and should not be read to indirectly prohibit a fund from using a profile as a selling document, a result that clearly would be at odds with the Commission's intentions regarding the profile.

<sup>23</sup> Rule 498(c)(2)(v)(B).

<sup>24</sup> The Commission should clarify that this would require funds to provide only minimum initial or subsequent investment requirements in the profile, not ongoing minimum account balance information. Providing disclosure about ongoing minimum account balance information could result in lengthy disclosure that would be inconsistent with the profile's purpose as a summary disclosure document. In addition, requiring funds to provide information about minimum initial or subsequent investment requirements in the purchase section of the profile would conform to the purchase information required by current Item 7 of Form N-1A and as that item is proposed to be amended. Further, under current Form N-1A and the proposed Form N-1A amendments, fund shareholders would be provided with information regarding "[t]he circumstances, if any, under which the Fund may redeem shares involuntarily in accounts below a certain number or value of shares" as part of the information provided about redemption of fund shares.

<sup>25</sup> See Items 8(a)(1) and 8(a)(2) of Form N-1A as proposed to be amended (requiring certain information about waivers of sales loads to be disclosed in the prospectus) and Item 13(e) of Form N-1A as proposed to be amended (requiring certain information about waivers of sales loads to be disclosed in the statement of additional information, or SAI). Proposed Rule 498(c)(2)(vi) does not distinguish between waivers that are required to be disclosed in a fund's prospectus and those that must be disclosed in the fund's SAI. We believe it would be particularly inappropriate to require more detail about waivers in the profile than what is required to appear in the fund's long-form prospectus.

<sup>26</sup> See Special NASD Notice to Members 95-80 (September 1995).

<sup>27</sup> See Item 7(b) of Form N-1A as proposed to be amended (requiring disclosure of the circumstances under which redemption charges may be waived); and Item 8(a)(2) and Item 13(e) of Form N-1A as proposed to be amended (both of which are described, *supra*, at note 25).

<sup>28</sup> Under rule 497(k)(3), a fund would be required to file a definitive form of profile electronically with the Commission, and under proposed Rule 497(k)(5) a fund would be required to send to the Commission two additional copies of a form of profile filed electronically in the primary form intended to be used for distribution to investors (e.g., paper). This second filing requirement would expire on March 10, 1999. Because Rule 101 of Regulation S-T requires funds to make substantially all of their required filings with the Commission electronically, funds no longer have procedures and personnel in place to accommodate paper filings. We note that if the proposed requirement is adopted, funds would be forced to make such accommodations to file profiles in paper.

<sup>29</sup> See Form N-1A Letter.

<sup>30</sup> To implement this recommendation, Rule 498(b)(2) would need to be modified to read as follows: "The Fund or, if applicable, the appropriate financial intermediary, responds reasonably promptly to a request for the Fund's prospectus, annual or semi-annual report, or Statement of Additional Information by first-class mail or other means designed to assure equally prompt delivery. For this purpose, "reasonably promptly" normally will be deemed to be within 3 business days of receipt of the request by the Fund or the financial intermediary." This suggested rule change reflects our recommendations regarding financial intermediaries which appear at p. 7. See also Form N-1A Letter (making a consistent recommendation regarding requests for the Statement of Additional Information and shareholder reports.)

<sup>31</sup> See Release at pp. 14-15. The Commission also should make clear that a fund's failure to comply with the reasonably promptly/normally 3 business day requirement in a given situation would not call into question the fund's use of profiles generally, but instead would be deemed a violation of Rule 498. The general instructions to Rule 498 provide, in relevant part, that "[a] Fund may provide a Profile to investors . . . if: [t]he Fund responds within 3 business days to a request for a prospectus, annual or semi-annual report, or Statement of Additional Information. . . ." The quoted rule text suggests that a fund's use of profiles generally would be deemed impermissible in the event that a fund does not comply with the rule's delivery requirement on any occasion. We believe that such a harsh remedy is inappropriate and unnecessary.

<sup>32</sup> At year-end 1995, overall retirement plan assets, including 401(k) plans, other defined contribution plans, defined benefit plans, section 457 governmental plans, section 403(b) arrangements and IRAs, constituted 35.7% of all mutual fund assets. The Institute estimated that approximately 38% of all section 401(k) plan assets were invested in mutual funds, up from 31% in 1994 and 21% in 1993.

<sup>33</sup> Retirement plans must furnish to participants a summary plan description ("SPD") written in a manner calculated to be understood by the average plan participant. Information provided in the SPD includes, among other things, a description of plan benefits and conditions of eligibility to receive them, the identification of the sources of plan contributions (employer or employee) and the method by which calculated, the identification of the funding medium for plan assets, and the procedures to be followed in presenting claims for benefits. The SPD must be revised to reflect material changes to plan rules or supplemented by a summary of material modifications to the plan. See ERISA section 102 and 29 CFR Part 2520.

<sup>34</sup> See, e.g., Internal Revenue Code sections 401(a)(31) and 402(f), requiring plan administrators prior to making a plan distribution to provide a written explanation to the participant of the applicable rollover, tax withholding and other tax rules, such as the availability of income averaging. Additionally, if joint and survivor and preretirement survivor annuity requirements apply, both ERISA and the tax code require appropriate notices and waivers applicable thereto. See ERISA section 205 and Internal Revenue Code sections 401(a)(11) and 417.

<sup>35</sup> See Form N-1A Letter for our recommendations regarding compliance with the Form N-1A amendments.

<sup>36</sup> Funds currently using profiles are relying on a no-action letter issued by the Commission staff to the Investment Company Institute (pub. avail. July 31, 1996) ("1996 No-Action Letter"). That no-action relief, by its terms, will expire on July 31, 1997. The Institute plans to submit shortly a request that the Commission staff provide additional no-action assurances permitting funds to rely on the 1996 No-Action Letter until such time as the Commission requires compliance with any profile rules adopted.

<sup>37</sup> See Release at pp. 29-30 ("Rule 498 would not permit a profile to incorporate by reference the information included in the fund's prospectus or any other disclosure document filed with the Commission. The profile is designed to summarize prospectus information in a self-contained format that would assist an investor in making an investment decision or in deciding to request additional information. Permitting a fund to incorporate by reference into the profile information in the prospectus would mean that information in the prospectus would be considered to be part of the profile disclosure. This result would not be consistent with the purpose of the

profile, which is to offer investors the option to make an investment in a fund based solely on the information in the profile.") (Citations omitted).

<sup>38</sup> Cf. *Speilman v. General Host Corp.*, 402 F. Supp. 190, 203 (S.D.N.Y. 1975) aff'd 538 F.2d 39 (2d Cir. 1976) (stating that courts should not make a prospectus "something akin to walking across a minefield in which the slightest misstep means substantial liability").

<sup>39</sup> See Rule 498(b)(1) (requiring funds to include only the information specified by Rule 498(c)); Instructions to paragraph (b) of Rule 498 (stating that the profile is intended to be a standardized summary of key information in a fund's prospectus and instructing funds to avoid excessive detail). See also Release at p. 12 (where the Commission stated that "too much information could make the profile lengthy, complex, and difficult to understand."); and Release at p. 11 (the profile is intended to be a "standardized summary of key information disclosed in a fund's prospectus").

<sup>40</sup> Compare Release at p. 5 (describing the Form N-1A amendments "[seeking] to focus prospectus disclosure on essential information about a particular fund that would assist an investor in deciding whether to invest in that fund) and Release at p. 11 (The 9 items of required disclosure in the profile are intended to summarize key information in a fund's prospectus.)

<sup>41</sup> For example, the Commission might change the proposed profile rule to require funds to provide, if appropriate, disclosure regarding material pending legal proceedings, limits on transferability of fund shares, material obligations or potential liabilities associated with owning fund shares (not including investment risks), and if the fund does not expect to qualify as a regulated investment company under Subchapter M of the Internal Revenue Code, the tax consequences of not qualifying. This recommendation is based on our review of disclosure that funds would be required to provide in Part A of Form N-1A under the Form N-1A Release but not in the proposed fund profile. It bears emphasizing that, if the Commission adopts this course, its final profile rule must identify all those specific categories of information that funds would be required to incorporate into their summary. By the same token, we believe the Commission should not require negative disclosure about any of the suggested items. For example, if there were no material pending legal proceedings to which the fund, the fund's investment adviser, or the fund's principal underwriter was a party, that fund's profile would not include any information regarding material pending legal proceedings. See Form N-1A Letter for our recommendations regarding this disclosure in the long-form prospectus.

<sup>42</sup> Section 19(a) provides that: "No provision of this title imposing any liability shall apply to any act done or omitted in good faith in conformity with any rule or regulation of the Commission, notwithstanding that such rule or regulation may, after such act or omission be amended or rescinded or be determined by judicial or other authority to be invalid for any reason." For purposes of Section 19(a), registration forms and the accompanying instructions are considered to be "rules and regulations" of the Commission. See 17 CFR Section 230.130 (providing that the term "rules and regulations," as used in Section 19(a), shall include "the forms for registration of securities under the Act and the related instructions thereto"). Such a statement in the Release in combination with the requirement of Rule 498(b)(1) that "[t]he Profile contains only the information required or permitted by paragraph (c) of this section. . ." could help protect funds from claims simply alleging that the fund's long-form prospectus contains more information than the profile.

<sup>43</sup> Securities Act Release No. 6447 at 818. The Commission provided these assurances in the context of the then-new two part disclosure format which permitted incorporation by reference of the SAI into the prospectus. Because the profile proposal would not permit a fund's Section 10(a) prospectus to be incorporated by reference into the profile, the need for the Commission to provide these assurances in the case of the profile is even greater.

<sup>44</sup> Securities Act Release No. 6447 at 818.

<sup>45</sup> Securities Act Release No. 6479 (Aug. 12, 1983), 48 Fed. Reg. 37928, 37930 and Form N-1A Release at note 254.