May 20, 2004

Mr. Jonathan G. Katz
Secretary
U.S. Securities and Exchange Commission
450 Fifth Street, NW
Washington, D.C. 20549-0609

Re: Disclosure Regarding Portfolio Managers of Registered Management Investment Companies (File No. S7-12-04)

Dear Mr. Katz:

The Investment Company Institute[1] appreciates the opportunity to comment on the Securities and Exchange Commission's proposal to require registered management investment companies to provide enhanced disclosure of information regarding their portfolio managers.[2] The Commission's proposal would require a fund to disclose information relating to: (1) the members of a portfolio management team; (2) other accounts managed by the fund's portfolio manager; (3) the portfolio manager's ownership of securities in the fund and in such other accounts; and (4) the portfolio manager's compensation structure. The Commission's proposal is intended to provide greater transparency regarding portfolio managers, their incentives in managing a fund, and potential conflicts of interest that may arise when they or the advisers that employ them also manage other investment vehicles.

The Institute generally supports the Commission's objectives. We are concerned, however, that certain of the proposed disclosure requirements would not effectively accomplish their intended goals, inasmuch as they would result in overly voluminous disclosure that might not be very meaningful to shareholders and/or disclosure that could adversely affect portfolio managers' legitimate privacy interests. Our recommendations are intended to address these concerns, while still achieving the Commission's objectives.

In summary, our comments are as follows:

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[1] The Investment Company Institute is the national association of the American investment company industry. Its membership includes 8,632 open-end investment companies ("mutual funds"), 621 closed-end investment companies, 126 exchange-traded funds and 5 sponsors of unit investment trusts. Its mutual fund members manage assets of about $7.545 trillion. These assets account for more than 95% of assets of all U.S. mutual funds. Individual owners represented by ICI member firms number 86.6 million as of mid 2003, representing 50.6 million households.

[2] *See* SEC Release Nos. 33-8396; 34-49398; IC-26383 (March 11, 2004); 69 Fed. Reg. 12752 (March 17, 2004) (the "Proposing Release").

- The Institute supports the Commission's proposal to require prospectus disclosure about portfolio management team members, but notes that the proposed disclosure requirements would not work for larger management teams. Accordingly, we recommend that the Commission modify the proposal to permit funds with portfolio management teams that consist of more than five members to identify the five individuals with the most assets under management; provided, however, that disclosure should only be required of those individuals that manage at least ten percent of the fund's assets.

- The Institute supports the proposal to require funds to provide disclosure in their statements of additional information ("SAIs") regarding conflicts of interest related to the portfolio manager's dual management of the fund's investments and those of other accounts, but recommends that the Commission modify the proposal to require funds to disclose only the material conflicts that exist given the type of fund(s) and account(s) at issue.

- The Institute opposes the requirement to provide SAI disclosure of policies and procedures that address conflict of interest issues, and recommends instead that the Commission require disclosure stating that the fund and/or its adviser have policies and procedures in place designed to address the conflicts of interest identified, and that such policies and procedures have been approved and are periodically reviewed by the fund's board of directors.

- The Institute supports the proposal to require SAI disclosure of the structure and methodology of the portfolio manager's compensation, but recommends that the Commission modify the proposed definition of the term "compensation" in certain respects.

- The Institute supports the proposal to require SAI disclosure of securities that the fund's portfolio manager owns, but recommends limiting the disclosure to securities in the fund that is making the disclosure. At the very least, the proposal should be modified to require disclosure of securities owned in (a) the fund and (b) the fund and other funds and accounts that are managed by the fund's portfolio manager, in the aggregate.

- The Institute supports the proposal to require disclosure of securities ownership within prescribed dollar ranges, but recommends that the maximum dollar range be "over $100,000" instead of "over $1,000,000" as proposed.

- The Institute opposes the Commission's proposal to subject index funds to the proposed disclosure requirements by removing the exclusion currently available to index funds that have as their objective to replicate the performance of an index.

Our comments are discussed in greater detail below.

A. IDENTIFICATION OF PORTFOLIO MANAGEMENT TEAM MEMBERS

The Commission's proposal would require funds to identify in their prospectuses each member of a committee, team, or other group of persons associated with the fund's investment adviser that is jointly and primarily responsible for the day-to-day management of the fund's portfolio.[3] Currently, a fund that engages a committee, team, or other group to manage the fund's portfolio is only required to disclose that the fund's investments are managed by a group; it need not disclose the names of the members of the group.[4] The Commission's proposal would require funds to provide detailed information on each member of the portfolio management team, including the member's name, title, length of service, business experience, and role on the team.

The Institute supports the Commission's proposal to require more information about a portfolio management team than is currently required. We are concerned, however, that the disclosure requirements proposed by the Commission would not work for all management teams. In particular, while the proposed requirements may be appropriate for teams that consist of a relatively small number of members (*e.g.*, five or fewer individuals), when applied to larger management teams, the disclosure could become unwieldy and less meaningful to shareholders.[5] Indeed, so-called "research-driven funds," for example, may have portfolio management teams with as many as 60 individuals, each of which has responsibility for managing a specified portion of the portfolio. If these funds were required to identify and provide specific information on each and every team member of their management team, their prospectuses would be filled with page after page of information that would not be useful to investors, mainly because each individual team member typically would have responsibility for only a very small percentage of the fund's assets, thus making their individual identities and other individual information substantially less material to investors. This lengthy disclosure might distract investors' attention from more important information in the prospectus.

For these reasons, the Institute recommends that the Commission modify its proposal to permit funds with portfolio management teams that consist of more than five members to identify the five individuals with the most assets under management; provided, however, that disclosure should only be required of those individuals that manage at least ten percent of the fund's assets.[6] We believe this recommendation would enable most funds that utilize a large portfolio management team to achieve the Commission's goal of providing investors with

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[3] We presume that the Commission's proposal would not change the current standard whereby a fund with a single portfolio manager with supporting staff identifies and provides disclosure regarding the portfolio manager only.

[4] *See, e.g.*, Form N-1A, Instructions to Item 6(a)(2).

[5] We note that this concern is amplified by the fact that, under the proposal, the full panoply of proposed SAI disclosures discussed in this letter would be required with respect to each member of a team, including disclosures relating to other accounts managed, compensation structure, and securities ownership. *See, e.g.*, Proposed Items 5(a)(2) and 15 of Form N-1A.

[6] In unusual cases, such as research-driven funds, it is likely that no individual will meet the proposed ten percent threshold. We recommend that those funds could provide the disclosure currently permitted for funds with portfolio management teams. *See, e.g.*, Instructions to Item 6(a)(2) of Form N-1A.

enhanced information regarding the portfolio management team, without inundating them with extensive disclosure that may not be particularly relevant or meaningful.

B. DISCLOSURE REGARDING OTHER ACCOUNTS MANAGED, POTENTIAL CONFLICTS OF INTEREST, AND POLICIES AND PROCEDURES TO ADDRESS CONFLICTS

The Commission's proposal would require a fund to disclose in its SAI any other account for which the fund's portfolio manager is primarily responsible for the day-to-day portfolio management.[7] The proposal would also require the fund to describe any conflicts of interest that may arise in connection with the portfolio manager's management of the fund's investments, on the one hand, and of the investments of the other accounts, on the other. Moreover, the fund would be required to include a description of the policies and procedures used by the fund or the fund's adviser to address any such conflicts. Our comments on these proposed requirements are discussed below.

1. Conflicts of Interest

The Institute supports the Commission's goal of providing investors with information that alerts them to the types of conflicts that can arise when a portfolio manager simultaneously manages a mutual fund and other accounts. We have concerns, however, regarding the nature and extent of the proposed disclosure. First, we are concerned that the requirement to disclose *"any* conflicts of interest that *may* arise"[8] is overly broad and open-ended. As a practical matter, it is impossible to identify with certainty every possible conflict. Firms may decide to err on the side of caution and provide a laundry list of *all* conflicts that could occur, however remote the possibility of their occurrence. Such an overly comprehensive list would not be helpful to investors. To alleviate this concern, we recommend that the Commission modify the proposal to require funds to disclose only *material* conflicts of interest that exist given the type of fund(s) and account(s) at issue. Requiring disclosure of material conflicts that typically exist (such as in the areas of trade allocations, short sales, etc.) would more appropriately tailor the requirement to elicit more relevant and meaningful information.

Second, we are concerned that requiring SAI disclosure of the fund's or the fund adviser's policies and procedures that address the conflicts of interest described would in many cases result in excessive disclosure.[9] In our view, most fund investors would not find the details

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[7] Proposed Items 15(a) of Form N-1A and 21.1 of Form N-2.

[8] Proposed Items 15(a)(4) of Form N-1A and 21.1(d) of Form N-2 (emphasis added).

[9] We note, for example, that it is not uncommon for a large fund complex to have detailed and complex trade allocation policies and procedures that exceed 10 pages. Inserting these policies and procedures alone into a fund's SAI would greatly increase the size of the document; obviously, including descriptions of policies and procedures designed to address *all* conflicts of interest (or even all material conflicts, per our suggestion above) would have a far greater impact. The problem would be significantly worse in the case of funds with multiple advisers, such as so-called "manager of managers" funds, inasmuch as the Commission's proposal would require SAI disclosure for each portfolio manager identified by the fund.

of how the policies and procedures specifically address such conflicts particularly useful.[10] Moreover, the length and complexity of this disclosure would likely increase as firms develop and/or revise their policies and procedures pursuant to the Commission's recently adopted compliance program rules.[11]

To alleviate these concerns, we recommend that the Commission eliminate the proposed requirement to provide SAI disclosure of the fund's and the fund adviser's policies and procedures. Instead, we recommend that the Commission require the SAI to disclose that the fund and/or its adviser have policies and procedures in place designed to address the conflicts of interest identified, and that such policies and procedures have been approved and are periodically reviewed by the fund's board of directors.[12] This recommendation would address our concerns related to excessive and unnecessary disclosure, while achieving the Commission's objective of informing investors as to the nature of the conflicts of interest that exist, and ensuring them that such conflicts have been addressed by appropriate policies and procedures that have been approved by the fund's board of directors.[13]

2. Categories of Other Accounts Managed

The Commission's proposal would require a fund to disclose both the number of other accounts managed by the portfolio manager and the total assets in such accounts within each of the following four categories: (i) registered investment companies; (ii) other investment companies; (iii) other pooled investment vehicles; and (iv) other accounts. For each such category, the fund would also be required to disclose the number of accounts and the total assets in the accounts with respect to which the advisory fee is based on account performance.[14]

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[10] While some firms may decide instead to summarize their policies and procedures, many may decide not to do so because of potential liability and concerns about being second-guessed if certain items are not included in the summary. We also have concerns regarding possible inconsistent summary descriptions among funds that choose this option.

[11] *See* SEC Release Nos. IA-2204; IC-26299 (December 17, 2003); 68 Fed. Reg. 74714 (December 24, 2003). The adopting release for these rules notes that an adviser's compliance policies and procedures would be expected to include policies and procedures related to trading practices and allocation of investment opportunities among clients. *Id.* at 74716.

[12] The fund compliance program rule requires fund boards of directors to approve and periodically review the fund's and the fund adviser's policies and procedures. The rule also requires the fund to appoint a chief compliance officer who, among other things, will annually furnish to the fund's board a written report on the operation of those policies and procedures. *See* Rule 38a-1 under the Investment Company Act of 1940.

[13] In the Proposing Release, the Commission requested comment on whether the proposed conflicts of interest disclosure requirement is sufficient or whether the Commission should prohibit portfolio managers of registered funds from managing certain types of accounts. Proposing Release at 12755. The Institute would oppose any such prohibition. In our view, prohibiting a portfolio manager from simultaneously managing registered and non-registered investment products would have a detrimental impact on investors, as it would reduce their access to the expertise of certain portfolio managers. It would have a particularly disruptive and anti-competitive effect on smaller investment management firms that have fewer employees and may not have the resources to maintain separate staff for different types of accounts. We believe that the disclosure approach proposed by the Commission, combined with requirements under the compliance program rules, provide a sufficient and preferable way to address concerns about conflicts arising from a portfolio manager's management of different types of accounts.

[14] *See* Proposed Items 15(a)(3) of Form N-1A and 21.1.c of Form N-2.

The Institute supports the Commission's proposal to categorize the other accounts managed by a fund's portfolio manager, but we recommend that two of the proposed categories – "other investment companies" and "other pooled investment vehicles" – be combined, as they appear to overlap. For example, it seems that a private equity fund could be placed in either category. The Proposing Release does not explain how these two categories are meant to be defined or why breaking them out separately would be helpful in achieving the Commission's objective of enabling investors to assess the conflicts of interest to which a portfolio manager may be subject as a result of managing a fund and other portfolios.[15] Accordingly, we recommend that the Commission combine the "other investment companies" and "other pooled investment vehicles" categories into one category, called "other pooled investment vehicles."

The Institute also recommends that the Commission clarify that the scope of the "other account" category includes only other accounts managed on behalf of the adviser that employs the portfolio manager. This clarification is necessary to avoid potential interpretive issues that could arise in situations such as when a fund's portfolio manager is managing an account in a personal capacity, *e.g.*, a family trust. We do not believe that the Commission intended for the proposal to be applied this broadly.

C. DISCLOSURE OF PORTFOLIO MANAGER COMPENSATION STRUCTURE

The Commission's proposal would require a fund to disclose in its SAI the structure of, and the method used to determine, the compensation received by its portfolio manager from the fund, its investment adviser, or any other source with respect to management of the fund and any other account included by the fund in response to the disclosure requirement discussed above.[16] The description would also have to clearly disclose any differences between the method used to determine the portfolio manager's compensation with respect to the fund and the methods used with respect to the other accounts. The purposes of the Commission's proposal are to help investors better understand a portfolio manager's incentives in running a fund and to shed light on possible conflicts of interest that could arise when the portfolio manager manages other accounts.[17]

The Institute supports the Commission's proposal. We particularly agree with the Commission's assessment that it is unnecessary to disclose the value of compensation paid to a portfolio manager.[18] In addition, with respect to the scope of the proposed disclosure, we agree

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[15] *See* Proposing Release at 12754.

[16] Proposed Items 15(b) of Form N-1A and 21.2 of Form N-2.

[17] Proposing Release at 12755.

[18] As the Proposing Release points out, the suggestion that portfolio manager compensation should be disclosed, just as executive compensation is for operating companies, ignores the fact that the closest analogue to executive compensation in the fund context is the advisory fee paid by the fund to the investment adviser. The advisory fee already is fully disclosed, including as part of the fee table in the fund's prospectus. *See* Proposing Release at 12755. We also point out that disclosing the value of portfolio manager compensation would raise privacy issues and

that salary, bonuses, deferred compensation, and certain retirement plan benefits would constitute the most significant aspects of a portfolio manager's compensation in order to help investors better understand the portfolio manager's incentives in running the fund, and therefore are appropriately included within the definition of "compensation" for this purpose.[19] We recommend modifications to the proposed definition, however, as it appears to be overly vague and broad in certain respects.

For example, it is unclear what the Commission intended to capture through the use of the phrase "without limitation" and by including "non-cash" compensation. Would the definition encompass healthcare and life insurance benefits or free parking? We do not believe that it should, because including these types of benefits would result in disclosure that would not achieve the Commission's purposes. On a related point, in order for the information to be useful to investors, the term "compensation" should have clearly defined parameters. This would promote consistent application and facilitate compliance with the proposed reporting requirements. For these reasons, we recommend that the Commission delete the phrases "without limitation" and "whether the compensation is cash or non-cash" from the definition.

In addition, certain benefits that are expressly included in the proposed definition – namely, qualified retirement plans and arrangements that meet certain IRS requirements and that are generally available to company employees – should not be covered because they are either fixed in amount, subject to a pre-set limit, or both. While a portfolio manager may receive such benefits as part of his or her compensation package, disclosing them would not assist investors in assessing whether the manager's interests are aligned with those of the fund's shareholders.

D. DISCLOSURE OF SECURITIES OWNERSHIP OF PORTFOLIO MANAGERS

The Commission's proposal would require a fund to disclose in its SAI the ownership of securities of each of its portfolio managers in the fund and in other accounts, including investment companies, managed by the fund's investment adviser or the portfolio manager.[20] The Institute's comments on this proposal are discussed below.

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consequently would act as a disincentive for talented portfolio managers to manage mutual funds, as opposed to other accounts (such as private accounts or hedge funds) that are not subject to such a requirement.

[19] The Commission's proposal would define "compensation" to include, "without limitation, salary, bonus, deferred compensation, and pension and retirement plans and arrangements, whether the compensation is cash or non-cash." *See* Proposed Instructions to Item 15(b) of Form N-1A and Item 21.1 of Form N-2. The proposal would also require funds to describe the criteria on which each type of compensation is based (*e.g.*, whether the compensation is fixed, based on fund pre-or after-tax performance over a certain period of time, and whether the compensation is based on the value of assets held in the fund's portfolio).

[20] Proposed Items 15(c) of Form N-1A and 21.3 of Form N-2. The proposed disclosure requirement would apply to securities owned beneficially or of record in: (i) the fund; (ii) other accounts that the fund included in response to the proposed disclosure requirements regarding other accounts managed by the portfolio manager; and (iii) any other account, including an investment company, managed by an investment adviser of the fund, or by any person directly or indirectly controlling, controlled by, or under common control with an investment adviser or principal underwriter of the fund.

Before providing our specific comments on the proposal, however, we would like to discuss our concern with the implications of the explanation in the Proposing Release that disclosing the shares owned by a fund's portfolio manager in the fund and in other accounts could help investors, among other things, *assess the level of confidence that the manager has in the fund's investment strategy*.[21] While the level of ownership arguably may be an indicator of the portfolio manager's confidence in the fund's investment strategy where the manager owns shares in the fund, it does not necessarily follow that a portfolio manager with little or no securities ownership has any less confidence or is any less concerned about the fund's performance than is a manager who has a large stake in the fund that he or she manages. There are a number of personal and professional reasons why a portfolio manager may decide not to invest in a fund he or she is managing. For example, the fund's objectives may be inconsistent with the manager's personal investment goals.[22] In order to avoid creating any undue negative inference, we urge the Commission to make clear in the adopting release that the level of the portfolio manager's investment in the fund is not necessarily indicative of the level of confidence the manager has in that fund's investment objective or strategies.

1. Securities Owned in Other Funds and Accounts

The Commission's proposal would require a fund to disclose in tabular format the ownership of securities of each of its portfolio managers in the fund and in other accounts, including investment companies, managed by the fund's investment adviser or the portfolio manager.[23] The proposal would require the fund to disclose the manager's securities ownership using the following dollar ranges: none; $1.00 - $10,000; $10,001-$50,000; $50,001-$100,000; $100,001-$500,000; $500,001-$1,000,000; or over $1,000,000. We have several comments on this proposal.

First, the scope of the proposal is overly broad. As drafted, the proposal would require the disclosure of a fund portfolio manager's ownership of securities not only in the fund being managed, but also in other accounts across the entire fund complex, including accounts over which the manager has no primary responsibility or control. The Proposing Release explains that this disclosure could help investors assess the extent to which the manager's interests are aligned with theirs and potential conflicts of interest between investors' interests and the interests of other clients or investment vehicles in which the manager has an interest. We fail to see, however, how this disclosure would achieve those goals. What conclusion should an

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[21] Proposing Release at 12755 (emphasis added).

[22] In addition, in response to recent events, many fund groups have adopted or are considering imposing restrictions, such as holding periods, that would apply to investments by portfolio managers in funds they manage. While such restrictions serve a worthwhile purpose, they may act as a disincentive for portfolio managers to invest substantial amounts in funds they manage.

[23] Specifically, the fund would disclose in a tabular format: (1) the name of the portfolio manager; (2) the investment company or account in which the portfolio manager or immediate family member owns securities; (3) the title of the class of securities owned; and (4) the dollar range of securities owned in the fund or account. *See* Proposed Items 15(c) of Form N-1A and 12.3 of Form N-2. For purposes of this disclosure, "immediate family member" would mean a person's spouse, a child residing in the person's household (including step and adoptive children), and any dependent of the person, as defined in Section 152 of the Internal Revenue Code.

investor draw from the fact that the fund's portfolio manager owns securities in other accounts in the complex, particularly those that he or she does not manage?[24] With respect to ownership of securities in accounts other than the fund managed by the portfolio manager, we submit that the other proposed disclosures concerning conflicts of interest (in particular, disclosure concerning compensation structure) would address the same purpose in a more direct and effective manner.

Second, the proposal is not adequately sensitive to portfolio managers' legitimate privacy interests. Requiring a fund to disclose its portfolio manager's holdings across the fund complex may raise privacy concerns in that it may provide too much insight into the manager's personal net worth, especially when coupled with the requirement to provide such information using a maximum dollar range of over $1 million. This disclosure would, in effect, require portfolio managers to disclose whether they are high net worth individuals.[25] This invasion of privacy could have the unintended effect of encouraging portfolio managers to move their investments to other fund companies in order to preserve their privacy. Such a move could adversely impact the firm's relationship with its portfolio managers, particularly if the firm promotes employee investment in the firm. Even worse, it could discourage talented investment professionals from serving as portfolio managers to mutual funds.

We recommend two changes to the proposal to address these concerns. First, we recommend that the proposal be modified to require a fund to disclose only the dollar range of securities owned in the *fund* by the fund's portfolio manager and his or her immediate family. At the very least, the proposal should be modified to require disclosure of securities owned in (a) the fund and (b) the fund and other funds and accounts that are managed by the fund's portfolio manager, in the aggregate.[26] This approach would be similar to the approach used for fund directors.[27]

Second, we recommend that the Commission reduce the maximum dollar range of securities owned to "over $100,000." We note that such a range would be consistent with the

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[24] The scope of the Commission's proposal would be even broader when applied to manager of managers funds. In such a case, the proposal would seem to require the fund to disclose the securities owned by a portfolio manager employed by a subadviser (or his or her immediate family members) in funds or accounts managed by any other subadviser to the fund, or by any entity that controls, is controlled by or is under common control with any other subadviser to the fund. For example, it appears that a fund would have to include shares owned by a portfolio manager's spouse through his or her 401(k) plan in a mutual fund managed by another investment advisory firm that happens to be a subadviser to the fund making the disclosures. Including this information within the scope of the required disclosure clearly would not serve the purposes intended by the Commission, and we do not think this result was intended.

[25] In this regard, we note that the Commission requested comment on whether the proposal should require a fund to disclose the percentage of a portfolio manager's net worth, including the net worth of immediate family members, that is invested in securities of the fund or other accounts. For the reasons stated in this section, we do not believe it would be necessary or appropriate to require a fund to disclose the percentage of a portfolio manager's net worth that is invested in securities of the fund or other accounts.

[26] As recommended in Section B.2 above, the other accounts should be limited to those managed by the portfolio manager on behalf of the adviser that employs the portfolio manager.

[27] *See, e.g.*, Item 12(b)(4) of Form N-1A.

requirement for fund directors.[28] We believe that a maximum threshold level of over $100,000 would provide an appropriate balance between two important competing interests – (1) providing information that would allow fund shareholders to assess the extent to which the portfolio manager's interests are aligned with theirs, and (2) avoiding undue invasion of portfolio managers' privacy.

3. Beneficial Ownership

The proposed securities ownership provision would apply to securities owned beneficially or of record. Specifically, the proposal would deem a person to be a "beneficial owner" of a security if the person is a "beneficial owner" under either Rule 13d-3 under the Securities Exchange Act of 1934, which focuses on a person's voting and investment power, or Rule 16a-1(a)(2) under the Exchange Act, which focuses on a person's economic interests in a security. The Commission has requested comment on whether the definition of beneficial ownership should be based on these two rules or limited to just one of them, and whether disclosure of record ownership should be required.

The Institute recommends using the Rule 16a-1(a)(2) definition to determine beneficial ownership and not requiring disclosure of record ownership. We note that the Commission took this approach when it adopted requirements for disclosure of directors' ownership of fund securities.[29] In deciding to require use of the Rule 16a-1(a)(2) definition in that context, the Commission stated: "In light of our objective of providing information about the alignment of directors' and shareholders' interests, we believe that disclosure of record holdings should not be required and that the focus of 'beneficial ownership' should be on whether a director's economic interests are tied to the securities, rather than his ability to exert voting power or to dispose of the securities."[30] We submit that the objective of the portfolio manager ownership disclosure requirement is very similar and, accordingly, it would be appropriate to use the same definition to determine "beneficial ownership" for that purpose and not to require disclosure of record ownership.

4. Calendar Year Reporting

The Commission's proposal would require funds to provide information about a portfolio manager's ownership of securities, as well as the information regarding other accounts

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[28] *See id.* While the Proposing Release recognizes that the proposed requirement is similar to that required for fund directors' ownership in equity securities, it suggests that the proposed higher ceiling of over $1 million (as opposed to over $100,000 for fund directors) is needed to differentiate between an investment of $100,001 and an investment of $5 million, which would both be stated as over $100,000 if that threshold were used. *See* Proposing Release at 12756. Nevertheless, we do not believe that this desire for greater precision outweighs the privacy concerns noted above – which apply to portfolio managers as well as directors. For these reasons, we urge the Commission to adopt the $100,000 threshold.

[29] *See* SEC Release Nos. 33-7932; 34-43786; IC-24816 (January 2, 2001); 66 Fed. Reg. 3734 (January 16, 2001) ("Fund Director Rules").

[30] *Id.* at 3741. The Commission further stated that the Rule 16a-1(a)(2) definition, consistent with this goal, "emphasizes the economic incidence of ownership." *Id.*

managed and compensation structure, as of the end of the fund's most recently completed fiscal year.[31] The Institute recommends modifying this proposal to permit funds to provide this information as of the most recently completed *calendar* year. It is not uncommon for fund complexes to have more than one of their funds and/or other accounts managed by the same portfolio manager. Imposing a fiscal year reporting requirement could cause such complexes to have to calculate and provide information on the portfolio manager based on different time periods, depending on each fund's fiscal year end. Permitting funds to make the calculation as of the end of the most recent calendar year would facilitate a more efficient process and provide greater consistency in reporting among those funds that have the same portfolio manager.[32]

E. REMOVAL OF EXCLUSION FOR INDEX FUNDS

The Proposing Release notes that the Commission intends to extend its proposed disclosure requirements to portfolio managers of index funds, which currently are excluded from portfolio manager disclosure. Specifically, the Commission proposes to remove the current provision in Form N-1A that excludes a fund that has as its investment objective replication of the performance of an index from the requirement to identify and provide disclosure regarding its portfolio manager. We disagree with this proposal and urge the Commission to maintain its longstanding exclusion for portfolio managers of index funds. As the Proposing Release explains, index funds were originally excluded from the disclosure requirement because their portfolio management is largely mechanical.[33] We note that this is still largely the case today.[34]

The Proposing Release explains that the Commission's decision to remove the exclusion for index funds is based in large part on concerns that conflicts may arise when a manager is managing both an index fund and an actively-managed fund that invest in some of the same securities.[35] In our view, however, subjecting the index fund to the disclosure requirement in that situation would serve little purpose inasmuch as there would be little or no conflict between the interests of the shareholders of the index fund and that of the portfolio manager where the fund's objective is to replicate the performance of an index. This is because the performance of an index fund is periodically measured and tracked against an identifiable

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[31] The Proposing Release notes, however, that in the case of an initial registration statement or an update to a fund's registration statement that discloses a new portfolio manager, information with respect to any newly identified portfolio manager would be required to be provided as of the most recent practicable date.

[32] We note that the Commission adopted a calendar year timeframe for reporting the dollar range of equity securities directors own in a fund complex. *See* Fund Director Rules, *supra* note 29.

[33] *See* Proposing Release at 12757.

[34] We recognize that index funds have evolved over the years to include "index plus" type funds, which have as their objective *out*-performing a specified fund index. Our comments focus, however, on the "plain-vanilla" index funds that have as their investment objective replication of the performance of an index. These funds, which typically do not have active managers who buy and sell securities based on research and analysis in an attempt to outperform a particular benchmark or the market as a whole, generally accomplish their objective by holding all, or a representative sample, of the securities that constitute the index in an attempt to mirror what the target index does.

[35] Proposing Release at 12757.

industry benchmark, which is clearly disclosed in the fund's prospectus. As such, the index fund structure imposes strict constraints on the portfolio manager's actions.[36] For these reasons, we urge the Commission to maintain the present exclusion for index funds that have as their objective to replicate the performance of an index.

F. COMPLIANCE DATE

The Proposing Release notes that once the proposal is adopted, the Commission expects to require all new registration statements and annual reports on Form N-CSR, and all post-effective amendments that are annual updates to effective registration statements, filed on or after the effective date to comply with the new disclosure requirements. We note that funds will need time to collect this broad range of information and ensure an adequate level of review of this new disclosure. To provide a sufficient transition period, the Institute recommends that the Commission provide a compliance date that is at least 12 months after adoption of the final rules. If the Commission does not narrow the required disclosures as we recommend above, however, a longer transition period may be necessary.

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The Institute appreciates the opportunity to comment on the Commission's proposal. If you have any questions concerning these comments or would like additional information, please contact me at (202) 326-5824, Frances M. Stadler at (202) 326-5822, or Barry E. Simmons at (202) 326-5923.

Sincerely,

Amy B. R. Lancellotta
Acting General Counsel

cc: The Honorable William H. Donaldson
The Honorable Cynthia A. Glassman
The Honorable Harvey J. Goldschmid
The Honorable Paul S. Atkins
The Honorable Roel C. Campos

Paul R. Roye, Director
Paul G. Cellupica, Assistant Director
Sanjay Lamba, Attorney
Division of Investment Management

[36] In this regard, we note that index funds are much like money market funds inasmuch as money market funds are also structured to impose strict constraints on the portfolio manager's actions. Indeed, it was on this basis that the Commission excluded money market funds from the disclosure requirement. *See* SEC Release No. IC-19382 (April 6, 1993) (excluding money market funds from the requirement to identify and provide portfolio manager disclosure because they must meet the risk-limiting conditions in Rule 2a-7 under the Investment Company Act, which constrains the role of the portfolio manager). The Proposing Release solicits comment on whether the Commission should subject money market funds to the proposed disclosure requirements. We believe that the current exclusion should be maintained inasmuch as the Commission's original justification for excluding money market funds still applies today.