**Securities Industry Association**

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June 6, 1997

Jonathan G. Katz
Secretary
U.S. Securities and Exchange Commission
450 Fifth Street N.W.
Washington, D.C. 20549

**Re: Investment Company Names - Release No. IC-22530**
**(File No. S7-11-97)**

Dear Mr. Katz:

The Investment Company Committee of the Securities Industry Association (SIA) **1** is taking this opportunity to comment on the above referenced release which contains certain rule proposals relating to the use of descriptive fund names to identify the principal focus of certain funds. These include funds which invest in securities of particular types, or in specific industry groups or geographic areas. This release is a "companion" release to two other simultaneously issued releases relating respectively to modification of Form N1-A and the proposed adoption of a "profile" prospectus. While, with minor exceptions, we strongly endorse the proposals contained in those releases, **2** the majority of our Committee have grave reservations concerning the functionality of certain aspects of the proposals relating to use of descriptive fund names.

## OVERVIEW

The proposed rule addresses two situations - fund names that may be "per se" misleading and those that are deemed to be misleading if the fund does not meet an 80% test regarding the focus of its investments. The former covers situations where terminology such as "government guaranteed" may be used to mislead an investor. The Committee generally supports this portion of the rule proposal, so long as it does not inhibit a fund from reasonably describing features of fund investments in the prospectus text which may guarantee face value at maturity or provide other benefits to investors. However, with respect to the 80% requirement, we believe that percentage tests are inherently flawed, will do a disservice to investors, have the contrary effect of preventing funds from achieving their investment objectives and will cause many funds to call shareholder meetings that will entail expenses disproportionate to any perceived benefits. Furthermore, we do not believe that these flaws can be overcome by including "temporary defensive position" provision in a percentage test.

## DISCUSSION

Given the thousands of funds and myriad investment strategies available, descriptive fund

names play an important role in the fund selection process, and the use of such names should not be discouraged. Unfortunately, proposed Rule 35d-1 will discourage such use because the 80% requirement will unduly inhibit fund managers from making investment decisions that they believe are in the best interest of their clients. Instead of managing for the purpose of achieving the best possible rates of return, their judgments may be subverted by a need to meet the percentage test regardless of the consequences for investors. While the proposed rule does provide for deviation from the 80% requirement through a "temporary defensive position" concept, this offers little comfort since "temporary" is not a term which lends itself to objective analysis. The inherent uncertainty, and opportunity for "second-guessing" a manager's judgment regarding the duration or severity of conditions which would warrant deviation from the0% standard would provide managers with far less latitude in basing investment decisions on judgments as to appropriate investments. Thus, the professional management process may come to be dominated by fear of litigation rather than exercise of investment acumen. Absent some clear indication of widespread abuse and investor harm, we believe that it is inadvisable to limit managers' ability to deal with issues of political instability, currency fluctuations, natural disasters and all of the other factors which may impact their investment decisions. We would respectfully suggest that instances in which investments have shifted away from the focus area, are largely the result of reactions to such events, and not in any way evidence of any intent to mislead investors. For this reason, we do not feel that the proposed percentage test is appropriate. Furthermore, the adoption of this rule is likely to impose additional burdens on the Commission to provide interpretations as to the circumstances under which diation from the standard is acceptable, and to what degree and for how long. To the extent the Commission does not or cannot address these matters, it appears unfortunately that only litigation will. This would have a chilling impact on managers' free exercise of their best investment judgment.

In addition, we also are concerned that adoption of the proposed 80% test will exact a significant price from investors in many funds which is unwarranted. Many funds created since the staff of the Commission adopted the 65% test in connection with fund names have made the 65% requirement a fundamental investment policy or restriction. In these cases, and because open-end funds no longer hold annual shareholder meetings, it would be necessary to call special meetings or shareholders to consider changing such policies or restrictions. Similarly, special meetings are likely to be called in many cases to the extent that funds would need to change their names to comply with the proposed 80% limitation. Fund investors will bear the cost of these special meetings. We believe that in most, if not all cases, these changes will not provide benefits to investors sufficient to justify the related expenses.

## CONCLUSION

For all of the foregoing reasons the Committee believes that the 80% test incorporated in proposed Rule 35d-1 will inhibit free exercise of professional investment management skills to the detriment of public investors. Its flaws cannot be redeemed by a workable "temporary defensive position" provision. Therefore, the 80% requirement, should be deleted from the final rule, and only that portion of the rule addressing names that are "per se" misleading should be adopted. This latter portion of the rule should be sufficient to address those relatively rare abusive situations where a fund makes no meaningful effort to focus investments in a manner suggested by its descriptive name.

We appreciate the opportunity to comment. Questions regarding this letter may be directed to

either Michael D. Udoff, Staff Adviser to SIA's Investment Company Committee, at (212) 618-0509 or to myself at (212) 783-5984.

Sincerely,

Lawrence H. Kaplan, Chairman
Investment Company Committee

**cc:**
Barry P. Barbash, Esq.
David U. Thomas, Esq.

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## Footnotes

**1** The Securities Industry Association brings together the shared interests of more than 760 securities firms throughout North America to accomplish common goals. SIA members -- including investment banks, broker-dealers, specialists, and mutual fund companies -- are active in all markets and in all phases of corporate and public finance. In the U.S., SIA members collectively account for approximately 90 percent, or $100 billion, of securities firms' revenues and employ about 350,000 individuals. They manage the accounts of more than 50-million investors directly and tens of millions of investors indirectly through corporate, thrift and pension plans.

**2** We have collectively addressed those releases in a separate comment letter dated June 6, 1997.