

June 30, 2000

Mr. Jonathan G. Katz
Secretary
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549-0609
(Filed electronically in Word format: rule-comments@sec.gov)

RE: File No. S7-09-00

Dear Mr. Katz:

The North American Securities Administrators Association (NASAA)¹ appreciates the opportunity to comment on the proposed rule and form amendments under the Securities Act of 1933 and the Investment Company Act of 1940 to improve disclosure to investors of the effect of taxes on the performance of open-end management investment companies.

Background

The Securities and Exchange Commission (“Commission”) requires that mutual funds disclose to prospective investors in narrative form the potential tax consequences of their investments. The Commission also requires that mutual funds provide investors information about portfolio turnover, prior year dividends and capital gains distributions. While useful, this information requires considerable effort for a prospective investor to assess the tax consequences of investing in a particular fund relative to other investment alternatives.

This lack of adequate disclosure combined with the often confusing subject matter and the financial impact on the investor has prompted a movement toward improved disclosure of the tax consequences of mutual fund investments among the mutual fund industry, regulators and Congress.

¹ The oldest international organization devoted to investor protection, the North American Securities Administrators Association, Inc., was organized in 1919. Its membership consists of the securities administrators in the 50 states, the District of Columbia, Canada, Mexico and Puerto Rico. NASAA is the voice of securities agencies responsible for grass-roots protection and efficient capital formation.

Congressional Initiatives

Concern over the lack of adequate tax disclosures in mutual fund sales materials prompted congressional inquiry. The findings of the House Subcommittee on Finance & Hazardous Materials exposed serious tax related investor protection concerns related to mutual fund performance disclosures,² including:

- That taxes can be the single biggest cost associated with mutual funds. The average stock fund investor loses up to three percentage points of return every year to taxes.
- Performance figures that mutual funds generally disclose to their shareholders are net of fees and expenses, **but not taxes**, and therefore do not represent the impact taxes have on an investor's return.
- Improved disclosure of the effect of taxes on mutual fund performance would allow shareholders to compare after-tax returns to raw performance, and would permit the investors to determine whether the fund manager tries to minimize tax consequences for shareholders.

On April 3rd, the House of Representatives passed and sent to the Senate, the "Mutual Fund Tax Awareness Act of 2000" (H.R. 1089), which mandated the Commission to evaluate workable solutions through the rulemaking process.

NASAA strongly supports this investor protection legislation which would allow the Commission to continue to strengthen their current rulemaking efforts in this area to require all mutual fund companies to clearly disclose in their prospectus language pertaining to after tax performance.

Proposed Rule and Amendments

NASAA, as an advocate for the main street investor, respectfully submits the following comments regarding the proposed rule and amendments.

The proposed rule and amendments would require mutual funds to disclose to investors the effect of taxes on the performance of open-end mutual funds. The funds would be required to disclose after-tax returns based on standardized formulas in advertisements and sales materials in order that the tax consequences of investing are realized prior to making an investment decision. NASAA concurs with the Commission that requiring this information to be computed according to a standardized formula would result in consistency of after-tax reporting and would minimize the economic burdens placed on the mutual fund companies who may be required to make these new prospectus disclosures. The Registered Representative representing the mutual fund could also be

² Congressional Record – House, April 3, 2000 at H1649.

called upon to assist the prospective investor and existing shareholder in understanding the new after-tax disclosure language.

NASAA also supports the proposed rule provisions requiring funds to disclose after-tax returns in a performance table contained in the prospectus. The additional requirement of a short explanatory narrative written in plain English regarding the disclosed returns will not only facilitate the understanding of this performance table but will lessen overall investor confusion.

NASAA supports these proposed provisions that improve disclosure and are designed to more effectively communicate the tax implications of mutual fund investing. NASAA believes that true financial disclosure is complete disclosure and these recommendations abide by this investor protection principle.

Conclusion

NASAA strongly supports this proposed rule and amendments that have already gained the imprimatur of Congress. NASAA believes that the proposed rule and amendments strike the appropriate balance between the responsibility of the mutual fund companies to disclose the potential after-tax factors that may be inherent with share purchases and the investor's right to be fully informed at the point of sale.

NASAA applauds the proposed SEC rule and amendments that protect the interests of mutual fund investors through disclosure of the relationship of tax consequences to performance prior to investment decisions being made.

NASAA appreciates the opportunity to provide guidance and comments in this area. If I can be of further assistance, please contact me directly at (317) 232-6695. Thank you.

Sincerely,

Bradley W. Skolnik
NASAA President
Indiana Securities Commissioner

