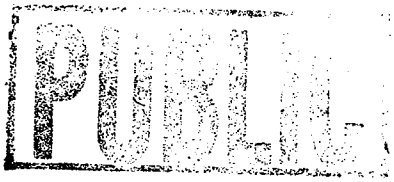
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549



February 3, 1997

ACT Securities Act of 1933
SECTION
RULE 482
PUBLIC AVAILABILITY Public

Dr. William Greene
Department Chair
Stern School of Business
44 West Fourth Street, Suite 7-88
New York, N.Y. 10012-1126

Dear Dr. Greene:

Commissioner Wallman has referred your inquiry regarding mutual fund performance to the Division of Investment Management, which, as you may know, is responsible for the regulation of the major participants in the investment management business. You ask whether a mutual fund sponsor can establish a number of lightly capitalized private pools for the purpose of generating performance track records. In the situation you describe, the sponsor, after waiting for a period of time, would select the pools with the best returns and take them public, touting their excellent past performance. You note that one of your colleagues suggested to you that the Commission staff recently took a position permitting this practice.

The hypothetical you raise is one that the Division terms the "incubator fund" problem. The Division has consistently, for close to thirty years, expressed severe reservations about these funds. In particular, the Division has been concerned that a mutual fund is likely to be managed differently than it was during its "incubation period" and that it is potentially misleading for a fund sponsor of a number of incubator funds organized at the same time to select and cite the performance of a single incubator fund without disclosing the performance of other similar, but less successful, incubator funds. These concerns underlie the Division's longstanding position that, to be consistent with the antifraud provisions of the federal securities laws, incubator fund performance should not be included in a mutual fund's prospectus in the absence of extremely clear disclosure explaining the sponsor's purpose in establishing the incubator fund. In view of this position, the Division is typically not even presented with the type of facts set forth in your hypothetical.

We presume that the staff position to which your colleague refers is a 1995 no-action letter to MassMutual Institutional Funds. Unfortunately, this letter has been, in our judgment, mischaracterized in a number of press accounts. In MassMutual, the Division permitted seven newly registered mutual funds to calculate past performance using performance data attributable to

their unregistered predecessor separate accounts. MassMutual, however, presented facts significantly different from those in your hypothetical. In particular, MassMutual represented that each predecessor account was created for purposes entirely unrelated to the establishment of a performance record. MassMutual noted, for example, that two of the separate accounts had been in existence for more than twenty years, two had existed for more than ten years, and the other three had each existed for at least four years. MassMutual also represented that each registered fund would be managed in substantially the same manner as its corresponding predecessor account. These representations were designed to ensure that a MassMutual fund's use of performance data attributable to an unregistered predecessor account would not mislead investors.

We believe that, in light of the facts presented in MassMutual, the relief granted in that letter in no way extends to the type of practice that you describe. Rather, such a practice would continue to raise serious concerns under the antifraud provisions of the federal securities laws.

I hope that this information is helpful. If you have additional questions, please call the undersigned, Barry A. Mendelson or Daniel E. Burton at (202) 942-0660.

Sincerely,

Jack W. Murphy
Associate Director
(Chief Counsel)

Enclosure