



May 21, 2004

*Via Electronic Filing*

Mr. Jonathan G. Katz  
Secretary  
Securities and Exchange Commission  
450 Fifth Street, N.W.  
Washington, DC 20549

**Re: Proposed Rule: Disclosure Regarding Portfolio Managers of Registered Management Investment Companies, Release Nos. 33-8396; 34-49398; IC-26383; File No. S7-12-04**

Dear Mr. Katz:

The Securities and Exchange Commission has proposed amendments to its forms under the Securities Act of 1933, the Securities Exchange Act of 1934, and the Investment Company Act of 1940 to improve the disclosure provided by registered investment companies (funds) regarding their portfolio managers.<sup>1</sup> The proposal would expand an existing requirement that a fund provide basic information in its prospectus regarding its portfolio managers to include the members of management teams. Funds would also be required to disclose additional information about their portfolio managers, including: (1) other accounts they manage; (2) their compensation structure; and (3) their ownership of securities in accounts they manage.

The Investment Counsel Association of America<sup>2</sup> strongly supports the goal of increasing transparency regarding the identity of portfolio managers, their incentives in managing a fund and the potential conflicts of interest raised by managing multiple investment accounts, and we applaud the Commission for issuing this important proposal. The ICAA supports the proposal with the comments and proposed modifications discussed below.

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<sup>1</sup> *Proposed Rule: Disclosure Regarding Portfolio Managers of Registered Management Investment Companies*, SEC Release Nos. 33-8396; 34-49398; IC-26383; File No. S7-12-04 (Mar. 11, 2004) (proposal).

<sup>2</sup> The ICAA is a not-for-profit association that exclusively represents the interests of SEC-registered investment advisers. Founded in 1937, the Association's membership today consists of more than 300 investment advisory firms that collectively manage in excess of \$4 trillion for a wide variety of institutional and individual clients. For additional information, please consult our web site at [www.icaa.org](http://www.icaa.org).

## 1. Identification of Portfolio Management Team Members

Funds are currently required to disclose basic information about the portfolio managers who are primarily responsible for the day-to-day management of the fund's portfolio;<sup>3</sup> however, funds are not currently required to disclose the identities of members of a portfolio team that manages the fund's portfolio.<sup>4</sup> The proposal would amend fund registration Forms N-1A and N-2 to require the disclosure of "each member of a committee, team, or other group of persons associated with a fund's investment adviser that is jointly and primarily responsible for the day-to-day management of the fund's portfolio."<sup>5</sup>

The ICAA supports disclosure of the proposed basic information about portfolio managers who have decision-making authority for the portfolio, regardless of whether the decision-maker is a single individual or several individuals who are part of a committee or team. We are concerned, however, that the definition of "jointly and primarily responsible" may be interpreted inappropriately to extend beyond members of a committee or team who have decision-making authority.

While portfolio management teams often include individuals who perform functions related to management decisions, such individuals are not necessarily empowered to make final investment or management decisions. For example, we understand that some portfolio management teams are made up of a combination of portfolio managers, who have equal authority to determine management decisions, and analysts, who have no decision-making authority. Moreover, the composition of a portfolio management team can be designed by an advisory firm to be flexible and members of teams who are not key decision-makers may be assigned among funds depending on the adviser's needs at a particular time.

Thus, there are several unfavorable outcomes that may result from a requirement to disclose information about every member of a portfolio management team.<sup>6</sup> A significant concern is that the most important information about key decision-makers may be obscured by lengthier discussions and less important information regarding every member of a team. Such a requirement could also inhibit an adviser's discretion to reorganize the composition of a team to the detriment of fund shareholders. Additionally, the costs associated with maintaining current disclosure would likely increase.

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<sup>3</sup> See Item 5(a)(2) of Form N-1A; Item 9.1.c of Form N-2 (requiring the name, title, length of service of the person or persons primarily responsible for the day-to-day management of the fund's portfolio, together with each person's business experience during the last five years).

<sup>4</sup> Instruction 2 to Item 5(a)(2) of Form N-1A and the Instruction to Item 9.1.c of Form N-2 require disclosure that a committee, team or other group of persons is primarily responsible for making the day-to-day management decisions of the fund, but not the names of the members of the group.

<sup>5</sup> Proposal at 4. The disclosure would include the portfolio manager's name, title, length of service, business experience for the last five years, and his or her role on the management team (*e.g.*, lead member).

<sup>6</sup> We also note that disclosure of individual members of a portfolio management team increases the likelihood of these individuals being solicited by competitors.

Accordingly, we ask the Commission to clarify that the term “jointly and primarily responsible” refers only to the individual members of a team or committee who are authorized to make final investment decisions for a fund’s portfolio.<sup>7</sup> Additionally, we ask the Commission to clarify that a fund that has designated a “lead member” of a portfolio management team or committee need only provide the proposed information about the lead member in the fund prospectus. Such a clarification would focus the required disclosure on the information most important to investors.<sup>8</sup>

Importantly, we recognize that this clarification may not be appropriate for every type of portfolio management team. For example, we understand that certain teams (*e.g.*, that manage research-driven portfolios) are comprised of many individuals (*e.g.*, as many as 25 or more), each of whom has decision-making responsibility for a small percentage (*e.g.*, less than five) of a particular fund. Disclosure regarding each decision-maker under these circumstances would yield the unintended result of pages and pages of unhelpful disclosure for that particular fund. This issue merits further consideration and we recommend that the Commission consult with industry participants to find a practical solution.

The Commission also requests comment on whether the proposal should include additional information about portfolio management teams and their members, such as the team’s structure and decision-making process.<sup>9</sup> We believe that the Commission has struck the right balance in this respect, primarily because additional information is not necessary and may increase the likelihood of detracting shareholders from more material information. As proposed, the requirements would permit an investment management firm to address further disclosure about the firm’s decision-making process on an individual basis.

2. Disclosure Regarding Other Accounts Managed, Potential Conflicts of Interest, and Policies and Procedures to Address Conflicts.

The proposal would require a fund to provide in its Statement of Additional Information (SAI) information regarding other accounts for which the fund’s portfolio manager is primarily responsible for the day-to-day management and any potential conflicts of interest that may arise in connection with the management of such accounts. The fund would also be required to provide a description of the policies and procedures used by the fund or the fund’s adviser to address such conflicts. The disclosure would include the total number of other accounts, the total assets in the accounts, and the number of accounts and

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<sup>7</sup> Proposed Instruction 2 to Item 5(a)(2) of Form N-1A and the Instruction to Item 9.1.c of Form N-2 appear to require the disclosure of each member of a portfolio team, regardless of the individual’s responsibilities. The proposed language reads “If a committee, team, or other group of persons associated with an investment adviser of the [Fund] is jointly and primarily responsible for the day-to-day management of the [Fund]’s portfolio, information in response to this Item is required for each member of such committee, team, or other group.”

<sup>8</sup> In the event the final amendments do require disclosure of members of a portfolio management team that are not authorized to make final decisions for a fund’s portfolio, we would recommend requiring disclosure about such individuals in the SAI.

<sup>9</sup> Proposal at 5.

total assets for which the adviser receives a performance-based fee.<sup>10</sup> This proposal would require the disclosure of applicable accounts by every member of a portfolio management team, including accounts managed by another portfolio management team that include an overlapping member of the fund's portfolio management team.<sup>11</sup>

The ICAA commends the Commission for proposing disclosure that is designed to enable 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. The proposed disclosure is an appropriate approach to mitigating conflicts of interest that are inherent in managing different types of accounts. While concurring with the approach, we recommend several clarifications to the proposal that we believe will result in more meaningful disclosure.

First, consistent with our prior comment, we suggest the proposed disclosure apply only to the individual members of a portfolio management team that are authorized to make final investment decisions for a fund's portfolio, and include only accounts for which that portfolio manager also has final investment decision-making authority.

Second, the proposal would require funds to describe any "conflicts of interest that may arise in connection with the [p]ortfolio [m]anager's management of the [f]und's investments on the one hand, and the investments of other accounts included [in the disclosure], on the other."<sup>12</sup> The ICAA strongly supports requiring the disclosure of conflicts of interest that result from a portfolio manager managing one type of account alongside another type of account. We are concerned, however, about the instructions to describe "any" conflicts that "may" arise. This broad terminology may cause funds to include lengthy lists of potential scenarios that could detract from actual material conflicts that exist. Accordingly, we ask the Commission to clarify the instructions to require disclosure of "material" conflicts of interest.<sup>13</sup>

Third, the proposal would also require a fund to either provide a description of its policies and procedures used to address conflicts of interest or to include a copy of the actual policies and procedures.<sup>14</sup> Given the potential for this requirement to overwhelm the

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<sup>10</sup> Proposal at 5-6 (describing proposed Item 15(a) of Form N-1A, proposed Item 21.1. of Form N-2, and proposed Item 22(a) of Form N-3). The term "accounts" would include registered and unregistered investment companies, other pooled investment vehicles, and other accounts. We note that the categories of "unregistered investment companies" and "other pooled investment vehicles" potentially overlap, and ask the Commission to clarify in the final release that each account need only be disclosed in one category.

<sup>11</sup> Proposed Instruction 2 to Item 15(a) of Form N-1A and Item 21 of Form N-2 reads: "If a committee, team or other group of persons that includes the Portfolio Manager is jointly and primarily responsible for the day-to-day management of the portfolio of an account, the account should be included in responding to ...this Item."

<sup>12</sup> Proposed Item 15(a)(4) of Form N-1A and Item 21.d of Form N-2.

<sup>13</sup> This clarification is consistent with an investment adviser's obligation to disclose conflicts of interest related to proxy voting. See *Final Rule: Proxy Voting by Investment Advisers*, SEC Release No. IA-2106; File No. S7-38-02 (Jan. 31, 2003) at Section II.A.2.b (requiring an adviser to have policies and procedures that address how the adviser resolves *material* conflicts of interest.) (emphasis added).

<sup>14</sup> Proposed Item 15(a)(4) of Form N-1A and Item 21.d of Form N-2 and accompanying instructions.

disclosure document, we believe it would be preferable to require disclosure that the fund has policies and procedures (approved and periodically reviewed by the fund board of directors)<sup>15</sup> that are designed to address conflicts of interest. At most, the fund should be required only to briefly summarize the policies, similar to the anticipated brief summaries that will be provided by advisers in Form ADV, Part 2 when it is adopted.<sup>16</sup>

The Commission has requested comment on whether a portfolio manager of a fund should be prohibited from managing certain other types of accounts.<sup>17</sup> The ICAA does not believe such a ban is necessary to protect fund shareholder interests because the disclosure is sufficient as proposed and consistent with an adviser's current fiduciary duty to disclose material conflicts of interests in all aspects of the advisory relationship. Additionally, advisers are required to have in place policies and procedures addressing such conflicts as part of their compliance programs.<sup>18</sup> Fund boards will have the relevant information to determine whether an investment adviser's policies and procedures addressing conflicts are appropriate to protect fund shareholders from inequitable treatment. Most significantly, we are concerned that prohibiting portfolio managers from managing certain other types of accounts would likely harm fund shareholders by limiting the pool of talented portfolio managers that would be eligible for, and interested in, managing mutual funds.

### 3. Disclosure of Securities Ownership of Portfolio Managers

The proposal would require a fund to disclose in a tabular format in its SAI the dollar range of securities owned beneficially or of record by the fund's portfolio manager in the fund and in other accounts 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.<sup>19</sup> The dollar ranges would be similar to, but exceed the current requirements of disclosure of fund shares for directors<sup>20</sup> and would apply to the portfolio manager and his or her immediate family members.<sup>21</sup> The stated purpose of this

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<sup>15</sup> Investment Company Act Rule 38a-1.

<sup>16</sup> See *Proposed Rule: Electronic Filing by Investment Advisers; Proposed Amendments to Form ADV*, Rel. No. IA-1862, File No. S7-10-00 (Apr. 5, 2000); Letter from ICAA General Counsel Karen L. Barr to SEC Secretary Jonathan G. Katz, submitting ICAA Supplemental Comments Regarding Proposed Amendments to Form ADV (May 24, 2001).

<sup>17</sup> Proposal at 7.

<sup>18</sup> *Compliance Programs of Investment Advisers and Investment Companies*, SEC Rel. No. IA-2204 (Dec. 17, 2003).

<sup>19</sup> Proposed Item 15(c) of Form N-1A and Item 21.3 of Form N-2.

<sup>20</sup> *Id.* The proposed highest dollar range (of over \$1 million) exceeds the highest range (of over \$100,000) currently applicable for fund directors. *Cf.* Instruction 4 to Item 12(b)(4) of Form N-1A; Instruction 4 to Item 18.7 of Form N-2.

<sup>21</sup> *Id.* The instructions to these items define "immediate family member" to include the individual's spouse, children residing in the individual's household, and any dependent of the individual as defined in section 152 of the Internal Revenue Code.

requirement is to allow fund investors to assess conflicts of interests and to determine the extent to which a portfolio manager's interests are aligned with fund investors.<sup>22</sup> We concur with these goals of the proposed rule, but recommend the following modifications to enable the rule to better achieve these aims.

First, consistent with our prior comment, we suggest the proposed disclosure apply only to the individual members of a portfolio management team that are authorized to make final investment decisions for a fund's portfolio, and include only accounts for which that portfolio manager also has final investment decision-making authority.

Second, we are concerned that the proposed disclosure could provide an incomplete or inaccurate picture regarding a portfolio manager's personal investment strategy. For example, little or no investment in a fund may simply reflect a portfolio manager's interests in addressing a competing investment need (*e.g.*, payment of student loans or other family obligations) and differing investment objectives. We suggest that this item should include cautionary language discouraging investors from interpreting a portfolio manager's disclosed holdings in a fund necessarily to be indicative of his or her alignment with fund shareholders or confidence level in the fund.

Third, we fully support the use of dollar ranges as opposed to actual dollar amounts. However, we are concerned that the proposed dollar ranges may compromise the privacy interests of portfolio managers by providing too much information about the manager's net worth, and cause fund managers who do want not this information to become public to choose not to manage registered funds. Thus, we recommend using dollar ranges identical to those now required for fund directors.

The Commission indicates that the purpose for proposing an increase in dollar ranges for portfolio managers as compared with fund directors is to alert fund shareholders of "significant" levels of investments and to allow a comparison of the "relative stakes of the manager in different accounts."<sup>23</sup> We believe any investment of \$100,000 or greater meets the threshold for "significance" and therefore that the current dollar ranges for fund directors appropriately address this concern. Further, depending on the circumstances, the relative stakes of the manager in different accounts may be more appropriately addressed as an aspect of material conflicts of interest in the "Other Accounts Managed" item of this section. Accordingly, we recommend that the "Ownership of Securities" section cross reference investors to the "Other Accounts Managed" section for more information about a portfolio manager's securities ownership interests in other accounts.<sup>24</sup> To avoid duplicative disclosure, this cross-reference would be in lieu of disclosure of other accounts in the "Ownership of Securities" section.

Finally, the Commission has requested comment on whether a fund should be required to disclose the percentage of a portfolio manager's net worth that is invested in the securities

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<sup>22</sup> Proposal at 8.

<sup>23</sup> Proposal at 9.

<sup>24</sup> See Proposed Item 15(a)(4) of Form N1-A and Item 21.1.d of Form N-2.

of the fund or other accounts.<sup>25</sup> We strongly believe that such a requirement is inappropriate and unnecessary. Similar to our concern over dollar ranges, we are concerned that such an invasion of privacy could deter talented portfolio manager from choosing to manage registered funds.

4. Disclosure of Portfolio Manager Compensation Structure

The proposal would require a fund to provide disclosure in the SAI regarding the structure of, and the method used to determine, the compensation of its portfolio managers. Specifically, the disclosure would require “a description of the structure of, and the method used to determine, the compensation received by a fund’s 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 proposed disclosure regarding other accounts managed by the portfolio manager.”<sup>26</sup>

The ICAA supports this disclosure as proposed. In response to the Commission’s request for comment, the ICAA does not believe that the disclosure of actual amounts of compensation received by portfolio managers is necessary or appropriate. However, we ask the Commission to provide further specific guidance on the definition and components of compensation required to be disclosed (*e.g.*, the extent to which they include health benefits or insurance policies).

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We commend the Commission for its thorough approach to addressing disclosure regarding portfolio managers. We would be pleased to work with the Commission to implement these initiatives and appreciate the opportunity to comment on the effects of the current proposal. Please do not hesitate to contact the undersigned or ICAA General Counsel Karen Barr to discuss any questions the Commission or its staff may have.

Sincerely,



Caroline Schaefer  
Associate 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

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<sup>25</sup> See Proposal at 10 (asking whether a fund should be required to disclose a percentage of a portfolio manager’s net worth that is invested in securities of the fund or other accounts).

<sup>26</sup> Proposal at 7-8. The proposed instructions provide the following examples of compensation: salary, bonus, deferred compensation, retirement plans and arrangements.