

Honorable Fred R. Harris
United States Senate
Washington, D. C. 20510

Dear Senator Harris:

In your letter of February 22, 1967 to Mr. Charles E. Thompson of Muskogee, Oklahoma, a copy of which you sent us and which we previously acknowledged, you invite us to comment on the points raised in Mr. Thompson's letter and on "The Investment Company Report -- An Emphatic Rebuttal" by Mr. William F. Shelley.

Mr. Thompson expresses concern with the ultimate impact of the recommendations contained in the Commission's Report on Public Policy Implications of Investment Company Growth on the profits of the securities industry. The Report has been printed as Report No. 2337 of the House Committee on Interstate and Foreign Commerce. Enclosed is a copy of the Commission's release announcing the filing of the Report with Congress, which contains a summary of the conclusions and recommendations set forth in the Report.

In its Report the Commission recommended that legislation be adopted placing a ceiling on the sales load which may be charged by dealers selling mutual fund shares. The reasons for this conclusion are summarized on page 7 of the enclosed release and are stated in detail in Chapter V of the Report, pages 221-223. There were two basic reasons for this recommendation. In the first place, sales charges for mutual fund shares are substantially higher than those generally prevailing for all other types of equity securities; and this may not only be harmful to investors in mutual fund shares but may also introduce various distortions into the growth and functioning of the securities markets by reason of what appears to be a disproportionate incentive on the part of dealers and their salesmen to sell mutual fund shares rather than other securities. This circumstance may also influence the judgment of dealers and their salesmen in selecting what securities they will recommend to their customers.

Moreover, the Commission concluded that competition did not function effectively to control the level of sales loads for two principal reasons. First, the mandatory resale price maintenance provisions of section 22 d, of the Investment Company Act of 1940 prevents retail price competition in the sale of the shares of any particular fund; and secondly, the type of competition which generally prevails in this area, i.e., competition among mutual funds and their underwriters for the favor of retail dealers rather than price competition between funds for the favor of individual investors, means that the general workings of competition tend to force sales loads up in order to attract the favor of dealers, not down in order to attract the interest of investors.

The release at page 8 also summarizes the Commission's recommendation, supported in much greater detail at pages 84-149 of the Report, that the Act be amended to provide expressly that all

compensation received by persons affiliated with a registered investment company shall be reasonable and to provide for judicial enforcement of this statutory standard.

We are returning Mr. Thompson's letter and its enclosure. Please write us again, if we can be of further assistance.

Sincerely,

Orval L. DuBois
Secretary

Enclosures

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SFREEDMAN
OLDuBOIS
DLRATNER