



Highlights of [GAO-03-909T](#), a testimony to the Chairman, Subcommittee on Capital Markets, Insurance, and Government Sponsored Enterprises, Committee on Financial Services, House of Representatives

Why GAO Did This Study

Concerns have been raised over whether the disclosures of mutual fund fees and other fund practices are sufficiently transparent and fair to investors. GAO's testimony discusses (1) mutual fund fee disclosures, (2) the extent to which various corporate governance reforms are in place in the mutual fund industry, (3) the potential conflicts that arise when mutual fund advisers pay broker-dealers to sell fund shares, and (4) the benefits and concerns over fund advisers' use of soft dollars.

What GAO Recommends

GAO's report recommends that SEC consider requiring additional disclosure by mutual funds of

- the fees that investors pay in account statements,
- revenue sharing payments that broker-dealers receive; and
- fund adviser's use of soft dollars.

www.gao.gov/cgi-bin/getrpt?GAO-03-909T.

To view the full report, including the scope and methodology, click on the link above. For more information, contact Richard Hillman at (202) 512-8678 or hillmanr@gao.gov.

MUTUAL FUNDS

Additional Disclosures Could Increase Transparency of Fees and Other Practices

What GAO Found

The work that GAO has conducted at the request of this Committee addresses several of the areas that are included in the recently introduced Mutual Funds Integrity and Fee Transparency Act of 2003 (H.R. 2420). Mutual funds disclose considerable information about their costs to investors, but unlike many other financial products and services, they do not disclose to each investor the specific dollar amount of fees that are paid on their fund shares. Consistent with H.R. 2420, our report recommends that SEC consider requiring mutual funds to make additional disclosures to investors, including considering requiring funds to specifically disclose fees in dollars to each investor in quarterly account statements, which we estimate may result in minimal increases in fund expenses. Our report also discusses other alternatives that could also prove beneficial to investors and spur increased competition among mutual funds on the basis of fees but be even less costly to the industry overall.

U.S. mutual funds have boards of directors who are charged with overseeing the interests of fund shareholders. Various corporate governance reforms have been proposed to improve the effectiveness of mutual fund boards. As a result of SEC requirements or industry best practice recommendations, many of these practices were already in place at many funds, but not all such practices were mandatory. H.R. 2420 would ensure that all mutual funds implement these practices.

Mutual fund advisers have been increasingly making additional payments out of their own profits to the broker-dealers that sell their fund shares. Although allowed under current rules, these revenue sharing payments can create conflicts between the interests of broker-dealers and their customers that could limit the choices of funds that investors are offered. Under current disclosure requirements, however, investors may not always be explicitly informed that their broker-dealer, who is obligated to recommend only suitable investments based on the investor's financial condition, is also receiving payments to sell particular funds. Consistent with H.R. 2420, our report also recommended that more disclosure be made to investors about any revenue sharing payments their broker-dealers are receiving.

Under a practice known as soft dollars, a mutual fund adviser uses fund assets to pay commissions to broker-dealers for executing trades in securities for the mutual fund's portfolio but also receives research or other brokerage services as part of the transaction. Although this research and other services can benefit fund investors, these arrangements could result in increased expenses for fund shareholders if fund advisers trade excessively to obtain additional soft dollar research. SEC has addressed soft dollar practices in the past and recommended actions could provide additional information to fund directors and investors, but has not yet acted on all of its own recommendations. Consistent with H.R. 2420, our report recommended that more disclosure be made to mutual fund directors and investors.