

John Rekenthaler, Leave it or Levitt, Morningstar.com (Oct. 6, 2000)

Dear Mr. Levitt:

Here's the good news. I love the job you've done as the chairman of the Securities and Exchange Commission. The bottom line--you think like an investor. In your seven years on the job, you've criticized Wall Street analysts for buttering up corporate managements, pushed companies to mark their derivatives positions to market, reformed NASD, and are currently battling the Big Five accounting firms because you believe their audits are compromised by their consulting businesses. Great stuff! No question, stock investors are better off for your efforts. You may be the ultimate insider, having founded Smith Barney and run the American Stock Exchange, but, unlike many SEC chiefs, you don't act the part.

For all these virtues, however, it seems to me that you've never quite understood mutual funds. Oh, you've done nice work on prospectus disclosure, jawboning fund companies to improve their wretchedly written prospectuses and to be clearer about the fees that they charge. But in general, these initiatives concern only an investor's *initial purchase decision*. Once a fund has been selected, you appear to believe that the work is pretty much done. As a result, you yawn at the notion that fund companies should reveal their portfolio holdings more frequently than twice a year. "Why bother?" you respond. "The effort wouldn't justify the cost."

Uh, what cost? Now that Al Gore has invented the Internet for us, the ongoing cost to fund companies for publishing portfolio holdings is roughly zero. Obviously, electronic files exist for all mutual funds. Just write some code to transfer those files to a Web site and, bingo! A fund's portfolio holdings can be updated at will. And yes, some people *do* care about using information that is less than six months old. I hear from them almost daily. More to the point, three mutual-fund competitors--separate accounts, Internet-based "folios," and exchange-traded funds--are proving in the marketplace that many people want to know what they own.

I imagine that you'll acknowledge these facts, and that you would have arrived at the same conclusion had you given the matter more than a cursory thought. But you didn't because, I believe, you don't really think of funds as "companies." Companies, as you so obviously know, must be carefully monitored, because they change their characteristics, manipulate the information they dispense to shareholders, and on occasion will even commit outright fraud. Just because an investor trusted a company six months ago doesn't mean that he or she should trust it today. That's why you, as SEC chairman, have pressed to make certain that stock investors who wish to be active and informed can be.

Well, mutual funds change their characteristics, too. Assets, portfolio managers, and investment trends come and go. Mutual funds have also been known to tell shareholders one thing, while doing something else. (In the mid-1990s, several bond funds were hit with lawsuits for promising conservative tactics while actually purchasing highly volatile mortgage-backed derivatives.) Sometimes, they have practiced actual fraud. Some mutual-fund investors also wish to be active and informed, Mr. Levitt. Let's treat them as they would wish--as owners of investment *companies*.