

asset value may not increase, the purpose of all investment is, after all, to enable the investor to secure capital appreciation and income. Thus, no investor should be expected to pay for losses due to heavy commissions on the first year of payment by contributing a portion of his capital appreciation for this purpose. The reasonableness of a commission, or the timing of its payment, should be measured by the amount actually invested, not by the prospects for later performance of the investment; to argue the contrary would justify higher than ordinary commissions on "growth" as against stable "income" stocks.

(C) Some have contended that the front-end load feature for mutual funds does not differ in substance from similar heavy commissions in early years to insurance salesman, or large early year interest payments on a house mortgage or other goods purchased "on time." The critical difference is that both the insured and the home owner have immediate enjoyment of the benefits or goods for which they have contracted. Death benefits for the insured who dies the next day are not scaled down, nor does the home owner receive only a half or some part of his house.⁵ In contrast, the purchaser of mutual fund shares under a front-end load plan finds that after one year of payments, his investment is only one half of the total amount paid. Moreover, the insured, besides getting full protection at once, also presumably receives, so long as he holds the policy, various services of his insurance agent, such as aiding him in processing a claim, etc. In contrast, once the front-end load plan has been sold, there is little more for the mutual fund salesman to do; and because the greatest part of the commission has been earned in the first year, he lacks economic incentive to work further with the investor under the plan or encourage his continuance. In short, the front-end load plan is essentially, and probably solely, a salesman's incentive to induce someone to initiate, but not necessarily to complete, the plan agreed upon.

3. Assuming that the prime reason for the front-end load plan is to quickly augment salesmen's commissions, it would be difficult to argue that this incentive is needed to promote the legitimate and desirable growth of the industry. Four major states—California, Illinois, Ohio, and Wisconsin—either prohibit or substantially regulate front-end load plans; and in California, which bars such plans, more mutual fund shares are sold than in any other state.⁶ This indicates that whatever incentive is afforded to salesmen, it is one which can and should be dropped, without serious detriment to the industry.

IV. SALES LOADS

(Section 12 of the Investment Company Amendments of 1967, amending Section 22 of the Investment Company Act of 1940)

The SEC has proposed key amendments to the 1940 Act restricting the sales load on mutual fund shares to a maximum of 5% of the amount actually invested in the fund. Because this is the most controversial provision of the bill and would, apparently, have widespread impact in the industry, I comment in detail on this provision, and particularly on the objections made to this proposal. I state at the outset that I endorse this proposal subject to the SEC's discretionary power to grant exemptions in appropriate situations.

1. The typical sales load of 8.5% measured as a percentage of the total amount paid by the customer (or approximately 9.3% of the amount actually invested in the fund) seems needlessly high. This 9.3% figure is roughly four and one-half times greater than the total commissions charged for a "round trip" (purchase and sales) of shares listed on the New York Stock Exchange.⁷ It contrasts unfavorably with the aggregate charges for purchase and sale of securities traded over-the-counter, on the basis of statistics from industry sources summarized in the SEC Study at page 212.⁸ Perhaps most markedly, it con-

⁵ The analogy with house purchases is also misleading, since the fact that a large proportion of early-year payments goes to interest simply reflects the fact that the loan is larger in early than in later years.

⁶ See *Investment Company News*, Vol. 7, No. 4 (April-May 1967), p. 3, for statistics on sales by states. 1966 California sales amounted to \$1,042,005,000, with New York second with sales of \$564,001,000.

⁷ This is nine times greater than the commission for a purchase alone. However, I agree that comparisons are properly made between the mutual fund sales charge (9.3%) and total commissions for a "round trip" since mutual funds redeem their shares without any charge or a miniscule charge at most.

⁸ "SEC Study" refers to *Report of the SEC on Public Policy Implications of Investment Company Growth* (1966), H. Rept. No. 2337.