THE UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Comments of:

Mr. Brent J. Fields
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Jeffrey Jarel Johnson
[redacted]

Re:

File No. S7-12-18
Request for Comments:
Fund Retail Investor
Experience and Disclosure

Submitted electronically on: October 31, 2018

To The United States Securities and Exchange Commission (herein, "SEC" or "Commission"):

These comments are provided in response to the Commission's rule proposing various enhancements to disclosures by mutual funds, exchange-traded funds ("ETFs"), and other types of investment funds (collectively, "Funds") to improve the investor experience and to help investors make informed investment decisions ("Request for Comment").[1] My name is Jeffrey Jarel Johnson, and I am pleased to submit these comments on my own behalf. My initial interest in this particular Request for Comment stems for my educational and professional background in securities regulation.

This comment will provide feedback on the current state of Fund disclosures. First, it will provide general comments on Fund disclosure documents. Second, it will summarize the main areas of concern and how the Commission and investment companies can remedy these issues. Next, it will examine three main areas of concern: (1) the delivery of Fund disclosures, (2) the design of Fund disclosures, and (3) the content of Fund disclosures. Within these three areas, it will provide detailed feedback on the investor experience and proffer multiple suggestions for the improvement of Fund disclosures. Finally, this comment will conclude with recommendations for the Commission and investment companies.

[1] Request for Comments: Fund Retail Investor Experience and Disclosure, 83 Fed. Reg. 26981 (purposed Jun. 11, 2018).

I. General Comments

The Commission proposes a multitude of recommendations within the Request for Comment.[2] However, the purpose of the Request for Comment is to gather information directly from investors. In total, the Request for Comment proffers one hundred and eleven (111) questions for investors.[3] While I will not answer all of the provided questions, I applaud the Commission for continuing to advance its mission of investor protection and maintaining fair, orderly, and efficient markets by requesting the comments and concerns of individual investors.

As the Request for Comment described, many Americans rely on Funds for important financial goals and milestones, such as saving for retirement, financing vacations, and funding their children's education.[4] Thus, it is imperative Fund investors understand their respective Fund's disclosure documents. In reality, this is not the case. Many Americans, including myself, are often lost in these dense and convoluted documents. Fund managers must improve the accessibility, readability, and delivery of all mandated disclosure documents. In order to promote the protection of passive investors, the Commission should promulgate more rules enhancing the readability of disclosure documents. The Commission mandates investment companies provide all material Fund information to investors through disclosures. However, a majority of the information is not useful to investors because they cannot comprehend the long documents filled with legalese and technical language. Thus, the Commission should encourage investment companies to simplify disclosures by integrating visual aids or cutting back on verbose statements.

II. Executive Summary

- The timing of Fund disclosure delivery can be improved by providing documents before an investor makes an investment decision.
    - An investor should be duly informed before making an investment decision.
    - Most disclosure documents are easily accessible because the SEC mandates annual SEC disclosures.
    - Investors prefer electronic delivery as opposed to physical delivery.
- The design of Fund disclosures can be vastly improved by improving writing techniques.
    - The plain English principle should be strictly enforced.
    - All disclosure documents should have a strict page and/or word limits.
    - The Commission should encourage the use of summary prospectuses and restructure Rule 498.
    - Funds should incorporate more visual aids in their SEC-mandated disclosure documents.
- The content of Fund disclosures can be improved by reformatting the sections of the disclosure.
    - The principal strategies and risks sections should appear earlier in the disclosure document and should adhere to a strict page and/or word limits.

---

[2] *Id*.
[3] *Id*.
[4] *Id*.

- The Commission should not create an exhaustive list of qualified principal investment strategies.
- The Commission should require a risk designation with a Fund's principal investment risks section of its disclosure documents.
- When necessary, Fund documents should incorporate past performance and advertising disclaimers.

III. Delivery of Retail Fund Disclosures

A. Timing of Disclosure Delivery

12. Before deciding to purchase shares in a Fund, the most important information to an investor is the Fund's principal investment strategies, principal investment risks, past performance, and management costs, also referred to as fees and expenses. All of this information is imperative to the investment decision-making process for several reasons. First, the Fund's principal investment strategies provide the investor with the Fund's investment techniques. Investors must fully understand how their Fund plans to ensure steady returns. The principal investment risks are equally important. Although investment companies boast about their past performance, most companies do not provide guaranteed returns. Thus, passive investors must be fully aware of the Fund's associated risks. Next, a Fund's past performance is an indicator of future earnings. While it does not guarantee any future return, this information is a credible gauge for success. Lastly, management cost or the fees and expenses section is important information to an investor. In order to accurately estimate the return, an investor must be fully aware of the Fund's associated costs.

Again, it is imperative that all investors have this information provided to them before they decide to purchase shares in a Fund. Without this information, an investor does not have an adequate understanding of the Fund's mechanics. As previously mentioned, the mission of the Commission is to protect investors. Fund shareholders require this protection because they are passive investors in two different regards. First, Fund investors are passive in regards to their respective Fund's daily trading activities. Second, many Funds purchase minority stakes in the publicly traded companies, which means the investors have little to no control of the daily activities of the company. While providing disclosure materials before an investment decision is made may require more regulations on investment companies, it is not overly burdensome. Investment companies are required to provide prospectuses and summary prospectuses on annual basis.[5] Therefore, it is not a daunting of a task to provide ***potential*** investors with readily available information.

B. Method of Disclosure Delivery

17-19. Technology has vastly improved access to Fund information. As aptly pointed out by the Request for Comment, ninety-five percent (95%) of individuals that own a share of a Fund have access to the internet.[6] While I cannot speak for the majority, it is reasonable to

---

[5] 17 C.F.R. § 270.30e-1.

[6] Request for Comments: Fund Retail Investor Experience and Disclosure, 83 Fed. Reg. 26981 (purposed on Jun. 11, 2018) (citing to ICI Research Perspective: Ownership of Mutual Funds, Shareholder Sentiment, and Use of the Internet, Investment Company Institute, at 18 (Oct. 2017), available at https://www.ici.org/pdf/per23-07.pdf)

conclude that many investors, including myself, would prefer to receive Fund disclosure documents via electronic mail ("e-mail"). Personally, a majority of my investment research is performed online. Whether it is Bloomberg Businessweek, Forbes, or simply checking a stock's price via Google search, all of my personal investment research is conducted by using the internet. Similar to other investors, I tend to check the markets on a daily basis. Fox Business's television programming is a valuable research tool. However, I am unable to watch television during peak broadcasting hours. Thus, I must resort to periodically checking the markets online via smartphone or personal laptop.

24. Before making an investment decision, I thoroughly research the Fund or stock. In my experience, most Fund websites offer an abundance of information and resources. If investment companies are providing more information online, then the need for paper disclosure documents is obsolete. As previously stated, the disclosure documents are dense, lengthy, and filled with legal jargon, which makes the documents hard to conceptualize for the average investor. On the contrary, online disclosure documents are much easier to understand with the help of the "Find" feature. Additionally, many investment companies provide shorter disclosure materials with graphs, tables, and charts, referred to as "fund fact sheets" (herein, "Fact Sheets"). Personally, Facts Sheets have been quality sources of information. However, Fact Sheets tend to resemble advertising materials and do not adequately explain the associated risks inherent to invest in a financial product. Thus, Fact Sheets are a good starting point for research.

The elimination of paper disclosure documents benefits the investment companies and investors. First, investment companies will reduce management cost. Additionally, investment companies will make a positive impact on the environment by reducing their carbon footprint. Investors can benefit from the reduction of dense materials and the incorporation of electronic delivery. In conclusion, the shift from paper to electronic disclosures benefit all parties.

IV. Design of Retail Fund Disclosures

A. Plain Language

33. As previously discussed, a Fund's disclosure documents are lengthy legal documents filled with technical language. The SEC and investment companies must remember their audience when comprising these materials. Disclosure materials are required to adhere to the plain English principles.[7] However, this requirement is not reflected in practice. In order to enhance readability and protect investors, the SEC should review all disclosure documents to determine whether the documents follow the plain English principles and penalize any document compromised of mostly legal and technical jargon.

35. The usage of the visual aids, including, but not limited to, charts, tables, and graphs, should be encouraged by the SEC. In my experience, Funds that incorporate visual aids enhance the readability of their disclosure documents. Again, investment companies must remember its audience. Many passive investors are not familiar with the technical language used in disclosure documents. In sum, most of the information within a disclosure document is ineffectual to the average investor because they cannot comprehend it. Thus, the SEC must promulgate rules encouraging or requiring the use of visual aids in disclosure documents. Additionally,

---

[7] 17 C.F.R. § 230.421 (d).

investment companies could incorporate additional visual aids in their respective advertising materials and websites.

B. Use of Summaries and the Summary Prospectuses

46. Prospectuses and summary prospectuses are essential documents to Fund shareholders. These documents contain all of the Fund's material information. As previously mentioned, the current securities laws require all Funds file a prospectus on an annual basis.[8] Thus, this information is relatively current and readily available. However, the summary prospectuses are much more useful to the passive investor. Distinguishable from a prospectus, a summary prospectus contains key information and omits the dense, and required, legal jargon contained in a prospectus.[9] In order to promote investor awareness and protection, the Commission should expand Rule 498 by allowing a summary prospectus to satisfy all sections 10(b)[10] and 24(g)[11] requirements for Funds.

50. As mentioned above, the increased usage of summary prospectuses is dependent on the increased accessibility. The most effective way to increase accessibility to summary prospectuses is to require electronic access or delivery. The 21st-century investor relies heavily on the internet for their information.[12] Similar to any other business, investment companies should cater to the needs of their consumers. An aggregation of Fund disclosures via e-mail will benefit investors by providing them with easy access to Fund information.

C. Structuring Disclosures

57. Similar to most Fund shareholders, my current usage of Fund data revolves around the annual disclosure documents. As previously mentioned, the principal strategies and risks, past performance, and fee and expenses sections are imperative to my understanding of a Fund's earning potential. However, Fund websites are becoming increasingly more informative. In terms of industry-wide trends and tendencies, the annual Investment Company Institute's Fact Book is a great resource.[13] Additionally, traditional broadcast mediums, such as business-orientated television programming, financial newspapers, and periodicals are excellent informational resources.

The SEC's website and EDGAR are largely under-utilized by the average investor. The SEC's website contains a plethora of information. However, it is not as user-friendly as other agency websites. Thus, the SEC could benefit by re-designing the website to cater to the investor. Although all of the requisite information is available on the website, it is difficult to navigate. The Commission should increase the size of the search bars, incorporate more buttons

---

[8] *Supra* n. 5.
[9] For more information regarding the classes, requirements, and contents of summary prospectuses, see 17 C.F.R. § 230.498.
[10] 15 U.S.C. § 77(e).
[11] 15 U.S.C. § 80a- 24(g).
[12] *Supra* n. 6.
[13] Investment Company Institute, *2018 Investment Company Fact Book*, ii (2018), available at https://www.ici.org/pdf/2018_factbook.pdf

and hyperlinks, and include more comprehensive Fund market data. Therefore, the individual investors will information presented in a more user-friendly manner.

58. The best way to project the profitability of a Fund is a market comparison. In theory, a fifteen (15%) return on equity ("ROE") does not mean much to an investor until he or she discovers the industry average ROE is between three (3) and five (5) percent. Comparative market data brings performance metrics into context. Investors would benefit from comprehensive Fund market data.

In order to compile this vast quantity of information, the Commission could work alongside financial lobbying groups, such as the Investment Company Institute, or lobbying firms such as the Smith-Free Group. Additionally, the Commission could designate an official advocate on behalf of individual investors. The incorporation of all interested parties ensures essential information is included in the comprehensive datasets. The Commission does an excellent job of collecting information through mandates. However, the comprehensive datasets should not be a rendition of the annual disclosures. Instead of simply dispensing massive amounts of data, the dataset should focus on the most impactful information for investors. The commission should summarize useful information and not produce yet another dense document filled with technical legal or financial jargon.

This type of information could increase the number of Americans that choose to invest in Funds. The Social Security system is in dire need of repair. As of now, younger Americans will not reap the benefits of Social Security. Most retired Americans rely on the Social Security for a majority of their income.[14] With concerns regarding the viability of the Social Security system mounting[15], the prudent young American will opt to invest into a Roth IRA and 401K for their retirement plan. An SEC-lead annual survey of the Fund market will give new investors additional resources, which could lead to an expansion of a twenty-two (22) trillion dollar industry.[16] In conclusion, the SEC, potential investors, and investment companies could benefit from comprehensive market data.

V. Content of Retail Fund Disclosures

A. Strategies and Risks

62. The federal securities laws require the disclosure of a Fund's principal investment strategies.[17] However, the summary of a Fund's investment strategies is not completely clear to the average Fund investor. While the necessary information is included, the Commission should focus on the readability of the disclosures and inquire into the usage of the plain English principles.[18] Bulleted lists convey the Fund's investment strategies in an informative and succinct way.

---

[14] Social Security Administration, *Fast Facts & Figures about Social Security,* p. 24-30 (2018), available at https://www.ssa.gov/policy/docs/chartbooks/fast_facts/2018/fast_facts18.pdf.
[15] *Id.* at 37.
[16] For more information regarding the size of the retail investment fund market, see *supra* n. 13.
[17] *See generally* 17 C.F.R. §§ 230.400-97 (providing general rules for disclosures); *See also*, Item 8 in Form N-2, p. 12.
[18] *Supra* n. 7.

The length is another glaring issue with the principal investment strategies section. As indicated by the Request for Comment, some principal investment strategy sections are over 5,000 words long.[19] This information is superfluous to the average Fund shareholder. Therefore, the SEC should promulgate strict page and/or word limits in this particular section of the disclosure. Moreover, a strict page and/or word limit for the entire disclosure document could enhance the overall readability of the disclosure document.

64. The establishment of specific criteria, guidelines, and thresholds for principal investment strategies is not an ideal remedial measure for disclosure documents because it may limit a Fund's ability to adequately describe their investment techniques. All investment companies are different. The stock market is a conduit of erratic human behavior. The establishment of rigid guidelines for principal investment strategies could hinder a Fund's ability to deal with the fluctuating stock market because Funds would be obligated to stay within a confined investment technique. Any deviation from a principal investment strategy would require an amendment to the Fund's disclosure materials.[20] In order to facilitate the effective trading of Fund shares, the SEC should not strictly categorize or define the term "principal investment strategy".

69-70; 72. Currently, Fund disclosures adequately describe the risk associated with investing. Similar to investing directly into the market, there is no guaranteed rate of return for most Funds. On the contrary, the higher risk associated with a Fund usually indicates a higher reward. When evaluating a Fund's risk, I always inquire into the industries or companies a Fund chooses to invest. Most Fund titles adequately inform the investor about the associated risks. For example, a Small-Cap Growth Fund will have more associated risks than a Large-Cap Value Fund because a growth Fund will target smaller companies with more earning potential.[21] In summary, a Fund's associated risks are easily identifiable.

In some cases, industry leaders, such as Fidelity, have created interactive visual tables, graphs, and charts.[22] These visual aids summarize essential Fund information. Visual aids are some of best disclosure tools. First, visual aids focus solely on the most important data. To passive investors, the underlying strategies are not as important as the overall results. A Fund shareholder trusts their investment company. Next, visual aids allow an investor to easily compare financial products. Fidelity incorporated all sixty-five (65) of their mutual funds into one interactive and cohesive tables.[23] Within this table, an investor can compare overviews, risks, management fees, Morningstar Rankings, and Income Characteristics of their financial products.[24]

---

[19] Request for Comments: Fund Retail Investor Experience and Disclosure, 83 Fed. Reg. 26981 (purposed Jun. 11, 2018).

[20] 17 C.F.R. §§ 270.0-3; 270.8b-15

[21] Small-Cap Growth mutual funds are comprised of securities of companies focused on capital appreciation, typically with a market capitalization between $300 million and $2 billion dollars. Large-Cap Value mutual funds contain securities of undervalued companies with high growth prospectus, typically with a market capitalization around $10 Billion.

[22] https://www.fidelity.com/fund-screener/evaluator.shtml#!&fdPks=Y&ntf=Y&expand=%24FundType&ft=DSTK_all&tab=mr

[23] S*upra* n. 22.

[24] *Id.*

Lastly, the SEC should incorporate a rating system, similar to the Canadian or European format, for the evaluation of a Fund's inherent risk. Again, Fidelity incorporates the Morningstar Ranking of each of its mutual funds.[25] The Commission should require all funds include its Morningstar rank within the principal risk section.[26]

While this may place additional administrative and financial burdens on the Commission and Morningstar, the Commission could elect to subsidize a portion of Morningstar's cost by promulgating the "Morningstar rating fee". In this context, the fee would require an annual payment by all investment companies for the increased costs of Morningstar risk assessments. Any failure of payment should lead to a financial penalty and a decreased rating.

B. Performance

84. As previously mentioned, past performance is a viable indicator of future earning potential. However, it does not guarantee returns. While some funds include past performance disclaimers, the SEC should draft and promulgate a standard past performance disclaimer. A multitude of factors could lead to a variation in a fund's annual performance including, but not limited to, changes in the market, technological advances, and Acts of God. Thus, past performance can mislead an investor into believing a fund will replicate its recent earnings. In conclusion, a clear and concise disclaimer would adequately warn all investors not to solely rely on past performance as an earnings indicator.

C. Fund Advertising

99-100. Facts Sheets are typically short pamphlets that summarize a fund's most important information. In most cases, Fact Sheets exalt the fund's returns, potential earnings, and fund managers. Conversely, Fact Sheets tend to dismiss the fund's inherent risks. Fact Sheets are a great place to start researching. However, they do not give an investor enough information to make a wise investment decision. Fact Sheets are useful for differentiating the small distinctions between funds. However, they do not provide as much information as a prospectus or a summary prospectus. Thus, an investor can be misled into believing a particular fund guarantees returns with little to no risk.

Fact Sheets are easier to comprehend than most SEC-required disclosure documents because they are shorter, more direct, and other focus on key disclosures. On the balance, an investor should not sacrifice readability over credibility. Fact Sheets are a marketing tool. Thus, the SEC should encourage the usage of fund Sheets but should require all investment companies include an advertising disclaimer for Fact Sheets.

[25] The Morningstar Risk Rating is a valuation conducted by investment research firm Morningstar. The ratings are given to mutual funds and ETFs on a scale from 1 to 5 stars based on their performance, after adjusting for risk and sales variables, in comparison to similar funds and ETFs.
[26] *Id*.

VI. Recommendations

- A prospectus and/or a summary prospectus should be provided to all potential investors.
- Other than the initial disclosure documents, all disclosure documents should be provided via e-mail. If an investor so chooses, the investor may receive elect to receive paper materials at a marginal cost.
- The SEC should promulgate rules imposing word and page limits on all fund disclosures.
- The SEC should encourage the use of summary prospectuses and redraft Rule 498 to include all funds.
- Online fund disclosures should incorporate more visual aids and informative hyperlinks.
- The SEC should provide a comprehensive market dataset of all essential fund information.
- The SEC should require past performance and advertising disclaimers.

VII. Conclusion

In conclusion, a vast amount of Americans own a share in a fund. These individuals are more than shareholders of a financial product. In many cases, these financial products are an individual's "nest egg". While this rule might place additional requirements on investment companies, the benefit of improving the investor experience is worthwhile. A few minor changes can produce many major positive results. I appreciate the opportunity to share my views on the state of fund investment disclosures and my investor experience.

Yours sincerely,

Jeffrey Jarel Johnson

cc: The Honorable Jay Clayton, Chairman

The Honorable Kara M. Stein

The Honorable Robert J. Jackson, Jr.

The Honorable Hester M. Peirce

The Honorable Elad L. Roisman