fund returns in a format that is simple and understandable. The Commission is particularly concerned that investors with long-term financial goals, such as those using mutual funds to fund a retirement plan, understand that money funds provide them with substantially less of an opportunity for long-term growth than other types of mutual funds.

Comment is requested whether funds should be required to compare their performance during each of the ten years with that of an index, and, if so, what type of index should be required for the comparison. Such a comparison would permit investors to compare how the fund performed relative to alternative investments or industry averages. For example, should money funds be required to compare their total returns to changes in the Consumer Price Index, or to a securities index? In order to foster comparability among funds, should the Commission prescribe the scale of the vertical and horizontal axes of the graph and other formatting specifications?

The Commission requests comment whether money fund investors are likely to use historical performance information when selecting a money fund. Alternatively, or supplementally, should the Commission require a short-term depiction of fund yield, such as a line graph comparing the fund's yield during the last twelve months with that of an index of short-term or money funds securities. Would investors find a line graph showing recent yields useful in money fund annual and semi-annual reports to shareholders, documents that focus on the more recent financial history of the fund? Should such a graph be substituted for the current financial highlights tables in those reports?

2. Descriptions of Investment Policies and Techniques

Item 4(a) of Form N–1A requires a fund to describe how it proposes to achieve its investment objectives. The Commission is proposing to amend this item to reduce substantially the amount of detailed, technical information regarding investment policies, techniques, and instruments now found in money fund prospectuses. In addition, this item would be reorganized to clarify its requirements.

Item 4(a)(ii) of Form N–1A currently requires ''a short description of the types of securities'' in which a fund invests, as well as any ''special investment practices or techniques'' used by the fund in connection with those securities and ''significant investment policies or techniques (such as risk arbitrage, repurchase agreements, forward delivery contracts, investing for control or management)'' that the fund uses or intends to use in the foreseeable future.[12] The responses to paragraphs (a) and (b) of Item 4 have become the longest and most complex section of many money fund prospectuses.[13] The responses often include detailed descriptions of numerous types of instruments, including U.S. Treasury bills and notes, government agency securities, short-term tranches of collateralized mortgage obligations and other types of asset-backed securities, certificates of deposit, bankers' acceptances, floating and variable rate securities, commercial paper, and repurchase and reverse repurchase agreements. The list is even longer for tax exempt money fund prospectuses, which may contain descriptions of variable rate demand notes; put bonds; general obligation bonds; bond, revenue, and tax anticipation notes; industrial development bonds; lease obligations; tax exempt commercial paper; and ''synthetic'' instruments, such as tender option bonds and custodial receipts. Descriptions of particular securities are often accompanied by lengthy descriptions of investment techniques, such as purchasing securities on a ''when-issued'' basis and acquisition of stand-by commitments.[14]

The following is a typical description of a portfolio security for a tax exempt money fund currently provided in response to Item 4(a):

> The Fund may purchase participation interests in municipal securities that have fixed, floating or variable rates of interest. These participation interests will be purchased from financial institutions that sell undivided interests in the securities that underlie the instrument. The Fund will only purchase such an interest if: (i) the underlying securities mature in twelve months or less or the instrument includes a right to demand payment (a ''demand feature''), usually exercisable within no more than seven days; (ii) the security meets certain quality standards set forth by the Fund and federal regulation; and (iii) the security is accompanied by an opinion of counsel or is the subject of a ruling from the Internal Revenue Service stating that the interest earned is exempt from federal income tax.

Another tax exempt money fund describes the investment technique of purchasing municipal bonds on a ''when-issued'' basis, also in response to Item 4(a), as follows:

> The Fund may purchase Municipal Obligations on a ''when-issued'' basis—the purchase of securities which are paid for and delivered beyond the normal settlement date. The Fund will generally not pay for such securities or start earning interest on them until they are received. Securities purchased on a when-issued basis are recorded as an asset and subject to changes in value based upon changes in the general level of interest rates. The Fund expects that its commitments to purchase when-issued securities will not exceed 25% of total assets, absent unusual market conditions, and that it will not commit to purchase when-issued securities beyond 45 days. The Fund does not intend to purchase when-issued securities for speculative purposes but only to further its investment objective.

To be eligible for money fund investment under rule 2a–7, the instruments described above all must be high quality and, although they may have different mechanisms for determining interest rates or maturity, all are designed to have the stability of principal and yield of short-term debt instruments. The riskiness of any particular investment technique is further limited by rule 2a–7's maturity and currency denomination conditions,[15] as well as the requirement that the board of directors adopt procedures designed to maintain a stable share price or net asset value.[16]

Because of the limitations on securities in which a money fund is permitted to invest, the particular types of securities in which a fund invests are unlikely to be an important factor for most investors when selecting a money fund.[17] Moreover, detailed, technical

[12] Item 4(b)(ii) (proposed instruction 3(ii) to item 4(a)) permits a fund simply to identify a practice if five percent or less of the fund's net assets are placed ''at risk'' by the practice. Money funds generally are not able to take advantage of this opportunity to simplify their disclosure because they require the flexibility to employ, above the five percent ''at risk'' level, many or all of the investment practices they describe.

[13] Some money funds, however, already limit those descriptions to general, basic statements about the securities in which they invest.

[14] Descriptions of particular types of securities (Item 4(a)(ii)(B)(1)) and various investment techniques (Item 4(a)(ii)(B)(1) and (D)) used by a fund often appear together in the same section of money market fund prospectuses.

[15] Rule 2a–7 limits the amount of currency risk to which money funds can be exposed by restricting their investments to U.S. dollar-denominated instruments. Paragraph (c)(3) of rule 2a–7. The rule limits the interest rate and credit risks to which money funds can be exposed by requiring that they maintain a dollar-weighted average portfolio maturity of no more than ninety days and generally invest in individual securities that have remaining maturities of no more than 397 days. Paragraph (c)(2) of rule 2a–7.

[16] See paragraph (c) of rule 2a–7.

[17] The Commission has considered whether disclosure of each type of security may provide investors with information they can use to avoid investment in money market funds investing in securities whose characteristics may threaten the fund's stable net asset value. In 1994 a number of fund advisers took steps to maintain the share values of money funds that had invested in adjustable rate securities that had interest rate adjustment formulas that did not result in the value