Ex-mutual fund CEO hits industry in book

Investing » Author is critical of the $11-trillion industry's fee practices and failure to keep shareholders informed.

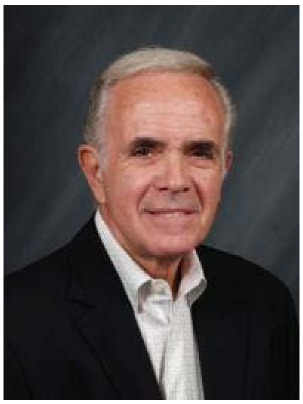
By Mark Jewell

The Associated Press

Updated: 10/22/2009 03:42:43 PM MDT

Dan Calabria, a former CEO of Templeton Funds before the company became Franklin Tempelton, has written a new book called "Mutual Funds Today: Who's Watching Your Money." (AP Photo/Dan Calabria)

Dan Calabria is a believer in mutual funds, imperfect as they may be: "I consider them to be the worst investment in the world, except for everything else that's out there," he quips.



His belief in the power of small investors pooling their money together is rooted in a fund industry career that spanned more than four decades, starting in 1963. Calabria rose through the ranks of Dreyfus and Oppenheimer Funds before becoming president and CEO at Templeton Funds for six years ending in 1992. He later left the executive ranks, serving as an independent director on boards for several funds.

So Calabria's not one you'd expect to self-publish a book noteworthy for its less-than-charitable descriptions of the $11-trillion industry's practices.

Check out the chapter and section titles in the newly published *Mutual Funds Today: Who's Watching Your Money* ? His take on shortcomings in keeping fund shareholders well-informed is titled "Shame on the Fund Industry." And then there's "12b-1 Fees -- The Multibillion Dollar Boondoggle."

Calabria, now 73 and retired in St. Petersburg, Fla., maintains fund companies often unfairly manipulate 12b-1s. The fees are paid out of a fund's assets -- aka investor money -- to cover costs such as marketing and sales, including advertising and compensation for brokers. The fees also can cover expenses to print and mail fund reports, or answer investors' questions.

Federal regulators gave the industry permission to start charging the fees in 1980 to help struggling fund companies recover from tough times in the 1970s. The fees were intended to temporarily offset costs to win back investors who had pulled out. But as the industry has grown, many offerings billed as "no-load" funds have relied on the fees to cover a variety of expenses and make up for their lack of upfront sales commissions.

Here are excerpts from a recent interview:

Q: What's your beef with 12b-1 fees -- especially now, when the industry is trying to recover from a market meltdown?

A: I think 12b-1 fees are justified, but only as they were originally designed to help the fund sales operations support a servicing effort -- to be there when the shareholder needs information, and to provide guidance.

But it's become bastardized. Portions of 12b-1 fees are now used for advertising and printing prospectuses. You can get situations where a company takes 12b-1 money for Fund A and spends those revenues to promote Fund B -- in other words, to promote the hot-selling fund. That's not fair to shareholders in Fund A.

I don't think the industry has done a good job explaining why the fees are there and why shareholders should pay for it. No matter whether the market is up or down, that money is coming in. And once a 12b-1 plan is adopted, the shareholders never have an opportunity to voice an opinion on it again. That's left entirely to the independent board directors of a fund.

Q: You criticize fund companies for taking too long to mail printed prospectuses. These days, information about performance, strategies and fees is readily available online. So why does mailing time matter?

A: It frosts me every time I get one in the mail. Last year I tracked how long it took me to receive prospectuses for seven funds I own, and I got them anywhere from 72 days to 82 days after the end date of the reporting period.

Most people throw them in the trash because it's stale news.

When it comes to annual reports, fund companies can have an accounting firm come in a couple weeks before year's end, do the bulk of its review then, and then fill in the blanks when the final numbers for the year are in. The final audit can be done within three weeks at most after the year is over. And then the annual reports can go out shortly after that.

Q: So why is there such a long lag time before investors get them?

A: The industry is working off the Investment Company Act that says you have 60 days to get out a report after the end of a reporting period. That law was written in 1940, when information flowed much more slowly. We no longer set print in hot type. Look at the *Wall Street Journal* -- within five days of a quarter's end, they publish a comprehensive report of fund performance. They can do that in five days. What am I missing?

Q: You last served as an independent director on a fund board a couple year ago, and now you say they're not sufficiently independent to act in shareholders' interests. How do you propose to fix fund boards?

A: When they start out, many independent directors have no experience in the industry. You need to know what the basics are, what's behind the facade.

I think anyone invited onto a fund board shouldn't have voting privileges their first two years, and their compensation should be at half the rate of experienced directors. And they should undergo continuing education to keep up on industry trends.

I think what in effect would be a two-year training program would serve everybody well. After two years, that director can understand the issues, and vote on anything in good conscience.

Dan Calabria bio

Occupation » Retired mutual fund executive

Age » 73

Home » St. Petersburg, Fla.

Career highlights » Started in 1963 with Dreyfus Funds in advertising and sales.

Joined Oppenheimer & Co. in 1965, eventually becoming executive vice president of its fund operation and a limited partner in the parent company.

Joined Lexington Funds in 1979.

Joined Templeton Funds in 1986 as president and CEO, responsible for sales, accounting, administration and shareholder services. Accepted a severance agreement in 1992 after Templeton was acquired by Franklin Funds, a deal that was a milestone in the history of Franklin Templeton Investments.

Helped organized William R. Hough & Co.'s Florida Tax Free Funds, a group of money-market funds, before retiring from the executive ranks in 1995.

Spent next 11 years serving as an independent director on boards for several funds.

Quote » "Let's admit the obvious -- there are altogether too damned many funds in the marketplace today. Where and when will it end? How did we get here? Simple -- the fund management business is very lucrative in that almost anyone can make money, lots of money, as long as you follow the rules and do what you say you'll do."

Just for fun » Before starting out in the fund industry, Calabria worked for a printing business. He tried to secure orders from the Dreyfus Fund to print its reports to shareholders. He didn't get the order, but ended up moving to Dreyfus as an assistant advertising manager.