

CORPORATE VERSUS CONTRACTUAL MUTUAL FUNDS:
AN EVALUATION OF STRUCTURE AND GOVERNANCE

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Abstract

This dissertation develops an analytic framework to evaluate the comparative merits of the structure and governance of the two dominant types of mutual funds -- the Corporate Fund (the U.S. model) and the Contractual Fund (the German, Japanese and British models). The former is characterized by centralized decision-making functions, while the latter employs a more decentralized structure. The semi-hierarchical structure of the Corporate Fund leads to significant transaction costs such as influence, intervention and collective-decisionmaking costs. Specifically, the board of directors is not effective in negotiating performance-related terms (e.g., fees), and shareholder suits based on fiduciary duties do not adequately address the thorny issue of who monitors the monitor. In addition, although shareholder voting on specific issues may be desirable, the concept of voting for directors is contrary to the realities of the mutual fund business. Therefore, the Corporate Fund has placed too much reliance on the board's discretion.

A conceptual analysis of the Contractual Fund demonstrates that its structural design and underlying rationales are fundamentally sound. Of the two Contractual Fund proposals considered by the SEC, the Unitary Investment Fund should be rejected because it provides no effective substitute for the board's oversight. The Unified Fee Investment Company proposal is a better alternative not only because competitive forces would adequately discipline with respect to its simplified fee schedule, but also because the

investment manager would be better motivated to coordinate a mutual fund's operations. This proposal can be further improved by shifting the regulatory focus to the investment manager and by substituting the board of directors with institutional monitors such as a trustee. Accordingly, the SEC should implement the proposal to promote organizational competition with the Corporate Fund.

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