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CORRESPONDENCE MEMORANDUM

DATE: May 3, 2007

TO: Wisconsin Deferred Compensation Board

FROM: Shelly Schueller, Director
Wisconsin Deferred Compensation Program

SUBJECT: Mutual Fund Industry Update

This memo provides an update on several developments in the mutual fund industry that may have a bearing on the investment options provided in the Wisconsin Deferred Compensation Program (WDC). These include news about Fidelity and an update on the ongoing American Funds cases.

Fidelity

Several years ago, the National Association of Securities Dealers (NASD) informed Fidelity that some of its equity traders and supervisors had accepted large travel, entertainment, gifts and gratuities (TEGG) from broker-dealers who execute Fidelity mutual fund trades. Fidelity's Independent Trustees authorized an independent investigation into this matter in July 2005.

In late 2006, Fidelity announced the results of the investigation. While the investigation could not prove that traders' receipt of TEGG did or did not result in excessive fund execution costs, it did conclude that certain traders had misdirected order flow among Fidelity's approved brokerage firms. The report on the investigation recommended that Fidelity pay the affected funds $40.7 million, plus interest and expenses of the investigation. Fidelity's Independent Trustees then increased this amount to $42 million, plus interest and expenses.

The Chair of Fidelity (E.C. Johnson III) issued a letter in which he apologized for the actions of Fidelity employees and agreed with the decision to pay the penalty. In its corporate statement, Fidelity also said:

> Fidelity Investments has cooperated fully with the Independent Trustees' investigation and concurs with the conclusion reached by the Trustees that "in spite of the absence of proof that the Funds experienced diminished execution quality" it is appropriate for Fidelity to make a one-time payment of $42 million plus interest to the funds. We will also separately reimburse the funds for expenses incurred by the Independent Trustees in the conduct of their review.

Copies of the Chair's letter, the corporate statement and the summary of the Independent Trustee's report are attached to this memo.

Fidelity will be at the May Board meeting to update the Board and answer any remaining

Reviewed and approved by David Stella, Deputy Secretary

Signature ______________________ Date ______________

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questions regarding this news and any other questions the Board may have.

American Funds
The EuroPacific Growth Fund, which is offered by American Funds Distributors (American Funds), opened to WDC participants on February 1, 2005. Shortly after the fund was opened to WDC participants, the NASD alleged that American Funds violated the NASD Anti-Reciprocal Rule by directing approximately $100 million in brokerage commissions to top sellers of the American Funds. American Funds has strongly denied the NASD allegation and believes there are no facts that support this allegation.

An NASD panel held a hearing on this matter in March 2006. On August 30, 2006, the hearing panel issued a decision in which it found that American Funds violated the rule in question. As a result, the NASD imposed a $5 million fine on American Funds. American Funds has stated that it strongly disagrees with this decision and has appealed the decision to the NASD's National Adjudicatory Council.

On November 22, 2005, the Superior Court of California in the County of Los Angeles dismissed another complaint against American Funds, which was made by the California Attorney General. The claim related to the sufficiency of disclosure of additional payments American Funds made to broker-dealer firms in recognition of the cost and efforts involved in educating financial advisers about American Funds. However, on February 7, 2006, the California Attorney General filed a notice that he will appeal the Court's decision. This is still pending.

Additionally, the American Funds was named as a defendant in certain class action lawsuits alleging that fees charged to fund shareholders are excessive. American Funds is also defending against these allegations.

Staff will continue to monitor each of the situations discussed in this memo and will keep the Board informed of any new developments.

Attachments