

STATE OF NEW HAMPSHIRE  
BUREAU OF SECURITIES REGULATION  
DEPARTMENT OF STATE  
25 CAPITOL STREET  
CONCORD, NH 03301

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FEB 27 2004

NEW HAMPSHIRE  
SECRETARY OF STATE

IN THE MATTER OF: )

Massachusetts Financial Services Company )

INV03-037 )

CONSENT AGREEMENT

For purposes of settling the above-referenced matter and in lieu of further administrative proceedings, Massachusetts Financial Services Company has submitted an offer of settlement, which the Bureau of Securities Regulation, Department of State, State of New Hampshire (hereinafter referred to as "the Bureau") has determined to accept. Solely for the purposes of these proceedings, and without admitting or denying the findings herein, the Respondent does hereby consent to the entry of this Consent Agreement as set forth below:

PARTIES

1. This action is brought by the New Hampshire Bureau of Securities Regulation on behalf of the State of New Hampshire pursuant to its authority under N.H. R.S.A. 421-B.
2. Respondent Massachusetts Financial Services Company ("MFS") is a Delaware corporation with headquarters in Boston, MA. MFS Fund Distributors, Inc. is a subsidiary of MFS and is a registered broker-dealer with a CRD # of 31052. MFS Fund Distributors, Inc. serves as a distributor for certain mutual funds for which MFS serves as an investment advisor.

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NEW HAMPSHIRE BUREAU  
OF SECURITIES REGULATION



## STATEMENT OF FACTS

After conducting a joint investigation with the Massachusetts Securities Division, the Bureau of Securities Regulation for the State of New Hampshire (hereinafter referred to as the "Bureau") says as follows:

1. MFS mutual funds, including MFS Series Trust II, Massachusetts Investors Trust, Massachusetts Investors Growth Stock Fund, MFS Emerging Growth Fund (Series Trust II), MFS Research Fund (Series Trust V), MFS Total Return Fund (Series Trust V), MFS Cash Reserve Fund (Series Trust I), MFS Government Securities, MFS Government Mortgage (Series Trust X), MFS Bond Fund (Series Trust IX), (collectively "Funds"), are all either open-ended management investment companies registered under the 1940 Act or investment portfolios or series within an investment company registered under the 1940 Act. Such funds are offered for sale by broker-dealers and other financial intermediaries which have entered into selling agreements with MFS Fund Distributors, Inc. Such funds are required to make notice filings with the Bureau of Securities Regulation.
2. MFS mutual funds are required to file one copy of their most recent printed prospectuses with the State of New Hampshire Bureau of Securities Regulation in connection with the annual renewal of their notice filings.
3. The prospectuses for the above listed funds filed in 2000 and 2001 contained the following disclosure statement under the heading Other Considerations – Excessive Trading Practices:

The MFS Funds *do not* (emphasis added) permit market-timing or other excessive trading practices. Excessive, short-term (market-timing) trading practices may disrupt portfolio management strategies and harm fund performance. [T]he MFS Funds reserve the right to restrict any purchase order (including exchanges) from any investor. To minimize harm to the MFS funds and their shareholders, the MFS funds *will* (emphasis added) exercise these rights if an investor has a history of excessive trading or if an investor's trading, in the judgment of the MFS funds, has been or may be disruptive to a fund.

4. The prospectus filed for each fund in 2002 and 2003 was modified slightly and stated as follows:



MFS Funds do not permit market timing or other excessive trading practices that may disrupt portfolio management strategies and harm fund performance.

5. The above quoted statements set forth the company's public disclosure regarding its prohibition of all "market-timing" activities with respect to its fund offerings for 2000, 2001, 2002 and 2003.
6. Despite and in direct contradiction to these public disclosures, for a period beginning at least in 1999, the company maintained an internal list of eleven "unrestricted funds" in which the company knowingly permitted market timing. This list was disseminated by MFS to certain broker-dealers. In so doing, MFS encouraged active market timing by certain individuals in these eleven funds.
7. MFS was aware of and even able to quantify the level of market timing it permitted in these funds as evidenced by an email from James V. Fitzgerald, president of MFS Distributors, dated May 14, 2003 in which he states that "We currently have approximately \$1.3 billion in known timer money at MFS."
8. Further, despite an indication in 2003 by Mr. Fitzgerald that MFS would no longer accept new market timing money, because "it can cause unnecessary trouble to an asset management company," the company adopted a policy that would allow existing timers to "leave their money in MFS, and continue to use our funds per the existing rules."
9. MFS further misled the general investing public by stating in its prospectuses for 2000, 2001, 2002 and 2003 that MFS Funds were to be purchased for "investment purposes only" since the investment objective for several of the Funds was "long-term growth of capital." In making this statement, MFS effectively created two classes of investors: buy and hold investors who were unaware of MFS's internal market-timing practices and a select group who used the Funds for market-timing to the detriment of the buy and hold investors.
10. MFS also misled the general investing public through its assurances that it would restrict, reject or otherwise place certain limitations on exchanges that were excessive. The reason MFS reserved the right to place these limitations was to protect shareholders from the adverse effects of frequent exchanges. In direct contradiction to its stated policies, MFS failed to exercise that right by allowing market timing to occur in these funds. Late trading also occurred within MFS funds. "Late trading" is the purchase of fund shares at the 4 p.m. closing price - but after the fund has legally closed for that day's trading. Such trading activity is the direct antithesis of the stated investment purpose of these funds. Despite MFS's public disclosure that MFS "will exercise its rights to restrict trades" if an investor engaged in excessive trading, late traders reaped substantial profits at the expense of other fundholders. MFS represents that this took place without the knowledge or consent of MFS.



11. Pursuant to Rule 11a-3 under the Investment Company Act, MFS allowed investors to trade freely within the MFS family of funds without incurring either "front end" or "back end" sales charges. In addition, investors who participated in broker-dealer wrap programs could trade in and out of the MFS fund family without incurring sales charges. These sales charge policies may have had the effect of making MFS funds desirable to market timers and late traders.
12. Investors were harmed by MFS's false and misleading statements in its prospectuses by being denied profits made available to market timers; by lost profits taken by such market timers; by the increased fees and transaction costs incurred by the funds to accommodate the market timers' trade activity; and the potential lost opportunity due to the need to maintain cash reserves necessary to facilitate the short-term trades.
13. Investors were misled by the fraudulent omission of a disclosure to the effect that MFS actually encouraged market timing in its funds by maintaining and selectively disseminating a list of market-timeable funds. Such an omission was material because of the significant volume of market-timing that occurred in these funds.
14. MFS unfairly benefited financially through its encouragement of market timing through the direct increase in management fees, which were based on a percentage of total assets under management and the indirect increase in management fees obtained from new investors who purchased the funds because of the appearance that MFS had more long-term assets under management than it actually controlled.

#### **STATEMENT OF LAW**

1. Pursuant to 421-B:3 it is unlawful for any person, in connection with the offer, sale, or purchase of any security, directly or indirectly to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading; or to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person.
2. Pursuant to 421:B19, it is unlawful for any person to make or cause to be made in any document filed under this chapter or in any proceeding under this chapter any statement which is, at the time and in the light of the circumstances under which it is made, false or misleading in any material respect or, in connection with such statement, to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading.



3. Pursuant to RSA 421-B:23,I, whenever it appears to the Secretary of State that any person has engaged or is about to engage in any act or practice constituting a violation of this chapter or any rule under this chapter, he shall have the power to issue and cause to be served upon such person an order requiring the person to cease and desist from violations of this chapter.
4. RSA 421-B:26,I provides that any person who knowingly violates any rule or order of the Secretary of State, may, upon hearing, except where another penalty is expressly provided, be subject to such suspension or revocation of any registration or license, or administrative fine not to exceed \$2,500 for each violation in lieu of or in addition to such suspension or revocation as may be applicable under this title for violation of the provision to which such rule or order relates.
5. Pursuant to RSA 421-B:26,III, any person who, either knowingly or negligently, violates any provisions of this chapter may, upon hearing, and in addition to any other penalty provided for by law, be subject to such suspension, revocation or denial of any registration or license, or an administrative fine not to exceed \$2,500 or both.
6. Pursuant to RSA 421-B:26,IV, all moneys collected as an administrative penalty under this chapter and all moneys collected pursuant to RSA 421-B:31, I(h) shall be credited to an investor education fund to be maintained by the state treasurer. Funds in excess of \$725,000 at the end of each fiscal year shall be credited to the general fund. The secretary of state, after deducting administrative costs, shall use moneys credited to that fund to provide information to residents of this state about investments in securities, to help investors and potential investors evaluate their investment decisions, protect themselves from unfair, inequitable, or fraudulent offerings, choose their broker-dealers, agents, or investment advisers more carefully, be alert for false or misleading advertising or other harmful practices, and know their rights as investors.
7. Pursuant to RSA 421-B:26,V, after notice and hearing, the secretary of state may enter an order of rescission, restitution, or disgorgement directed to a person who has violated this chapter, or a rule or order under this chapter. Rescission, restitution or disgorgement shall be in addition to any other penalty provided for under this chapter.

### SANCTIONS

In view of the foregoing, the Respondent agrees to the following undertaking and sanctions:



1. Respondent agrees that it has voluntarily consented to the entry of this Order and represents and avers that no employee or representative of the Bureau has made any promise, representation or threat to induce their execution.
2. Respondent agrees to waive its right to an administrative hearing and any appeal therein under this chapter.
3. Respondents agree to, by Order, cease and desist from future violations under this chapter pursuant to RSA 421-B:23.
4. Respondent agrees in connection with the resolution of this New Hampshire proceeding and proceedings brought by the Securities and Exchange Commission and the New York Attorney General, to make restitution to investors in the amount of \$225 million to be administered in accordance with the plan to be approved by the Securities and Exchange Commission.
5. Respondent agrees to pay an administrative fine in the amount of \$1,000,000 according to the provision of RSA 421-B:26 IV. Two hundred fifty thousand dollars of those funds shall be used for investor education purposes in the State of New Hampshire. Seven hundred fifty thousand dollars shall be contributed to the North American Securities Administrators Association, an organization that includes the 50 state securities agencies, designated for the Investor Protection Trust, and used for general public education regarding mutual funds.
6. Respondent agrees to designate a compliance officer who will implement and oversee a market-timing policy and its compliance procedures. The Compliance Officer will report directly to the independent board members and make period reports to the New Hampshire Bureau for a period of two years regarding the market timing policy and related issues.
7. MFS undertakes to recommend to the boards of trustees of MFS's U.S. registered funds (the "Funds' Boards") that the funds "sticker" the prospectus, that is, issue a prospectus supplement promptly upon entry of this Consent Agreement (i) disclosing the fact that MFS has settled civil administrative proceedings against MFS brought by the Securities and Exchange Commission, the Bureau of Securities for the State of New Hampshire and the New York Attorney General (the "Regulatory Authorities"); (ii) describing the charges brought against MFS by the Regulatory Authorities; and (iii) disclosing the amount of the penalties, fines and disgorgement MFS has agreed to pay and the nature of the remedial actions and governance reforms MFS and the funds have agreed to undertake, as part of those settlements.
8. Respondent agrees to defray the costs of this investigation, \$50,000 payable to the Bureau and \$50,000 payable to the Massachusetts Bureau of Securities Regulation.

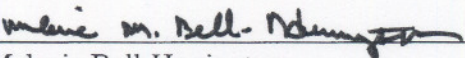


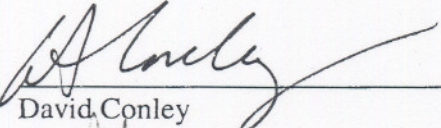
Based on the foregoing, the Bureau deems it appropriate and in the public interest to accept and enter into this Consent Agreement. **THEREFORE, IT IS HEREBY ORDERED THAT:**

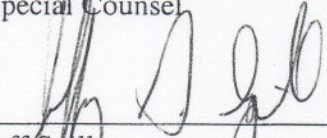
1. Respondent comply with the above-referenced undertakings.

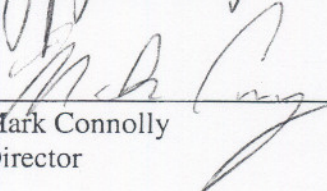
Executed this 2 day of March, 2004.

by:

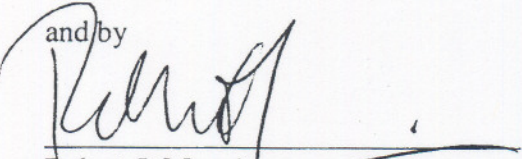
  
\_\_\_\_\_  
Date \_\_\_\_\_  
Melanie Bell-Harrington  
Special Counsel

  
\_\_\_\_\_  
Date \_\_\_\_\_  
David Conley  
Special Counsel

  
\_\_\_\_\_  
Date \_\_\_\_\_  
Jeff Spill  
Chief of Enforcement

  
\_\_\_\_\_  
Date \_\_\_\_\_  
Mark Connolly  
Director

For the Bureau of Securities Regulation

and by  
  
\_\_\_\_\_  
Date \_\_\_\_\_  
Robert J. Manning  
Director, Executive Vice President

for MFS