

money market fund shares at the net asset value would seem to provide little opportunity for insider self-dealing or overreaching, and thus an exemption from these provisions appears to be appropriate. We seek comment on this proposal. Does an acquiring fund's investment in an affiliated money market fund create other opportunities for self-dealing or overreaching?

(b) *Unaffiliated Money Market Funds.* Although our exemptive orders have permitted funds to invest their cash only in money market funds advised by the same adviser, we are proposing to expand that relief to funds that do not share the same adviser.<sup>43</sup> As a result, funds would be able to invest cash in money market funds that are members of other fund complexes. The exemption would permit funds in smaller complexes that do not have a money market fund to engage in a cash sweep arrangement.<sup>44</sup> Because of the nature of money market funds, which we discussed above, we do not believe that investments in money market funds that do not share the same adviser would create any greater risks than investments in money market funds with a common adviser.

If a fund acquires more than five percent of a money market fund's securities, the two funds would become affiliated persons of each other.<sup>45</sup> As a result, principal transactions other than purchases and redemptions of fund shares would not be exempt under the proposed rule, and thus the two funds would be precluded from entering into certain types of transactions with each other.<sup>46</sup> Moreover, the acquiring fund would be restricted with respect to the purchase or sale of securities through a broker-dealer affiliated with the money market fund.<sup>47</sup> We seek comment on

whether funds would be likely to invest cash in money market funds in other fund complexes? If so, would additional exemptive relief under the proposed rule be appropriate?<sup>48</sup>

(c) *Unregistered Money Market Funds.* Proposed rule 12d1-1 also would codify our exemptive orders that permit funds to invest in money market funds that are not registered investment companies ("unregistered money market funds").<sup>49</sup>

broker, in connection with the sale of securities to or by the fund, from receiving from any source a commission, fee, or other remuneration for effecting the transaction that exceeds specified limits. See 15 U.S.C. 80a-17(e)(2).

<sup>48</sup> We have provided relief for transactions between a fund and another entity that are affiliated as a result of the fund's investments in a money market fund that is affiliated with the other entity. See, e.g., Credit Suisse Asset Management, LLC, Investment Company Act Release No. 25789 (Oct. 29, 2002) [67 FR 67220 (Nov. 4, 2002)] (notice), Investment Company Act Release No. 25832 (Nov. 22, 2002) (order) ("Credit Suisse Notice and Order"). This relief generally has been provided in connection with applications regarding securities lending programs. We are considering separate rulemaking in this area that would address those issues.

<sup>49</sup> See, e.g., Pioneer America Income Trust, Investment Company Act Release No. 25607 (June 7, 2002) [67 FR 40757 (June 13, 2002)] (notice), Investment Company Act Release No. 25647 (July 3, 2002) (order) ("Pioneer Notice and Order"); Bear Stearns Funds et al., Investment Company Act Release No. 25467 (Mar. 20, 2002) [67 FR 13809 (Mar. 26, 2002)] (notice), Investment Company Act Release No. 25527 (Apr. 16, 2002) (order); GE Funds, et al., Investment Company Act Release No. 22187 (Aug. 29, 1996) [61 FR 46876 (Sept. 5, 1996)] (notice), Investment Company Act Release No. 22247 (Sept. 25, 1996) (order). The exemptive relief provided in these orders includes conditions requiring that: (i) The unregistered money market fund comply with rule 2a-7; (ii) the investment adviser to the unregistered money market fund (or the fund with approval of its board of directors) adopt and monitor the procedures described in rule 2a-7 and take any other actions required to be taken under the procedures; (iii) an acquiring fund purchase shares of an unregistered money market fund only if the unregistered money market fund's adviser determines on an ongoing basis that the unregistered money market fund is in compliance with rule 2a-7 and preserves for a period not less than six years from the date of determination, the first two years in an easily accessible place, a record of the determination and the basis on which it was made, and the record is subject to examination by Commission staff; (iv) the unregistered money market fund comply with the requirements of sections 17(a), (d), and (e), 18, and 22(e) of the Act as if it were a registered open-end fund; (v) the investment adviser to the unregistered money market fund adopt procedures designed to ensure that the fund complies with those provisions of the Act, periodically reviews and updates as appropriate the procedures, and maintains books and records describing the procedures; (vi) the investment adviser to the unregistered money market fund maintains the records required by rules 31(a)-1(b)(1), 31a-1(b)(ii)(2), and 31a-1(b)(9) under the Act for a period of not less than six years from the end of the fiscal year in which any transaction occurred, the first two years in an easily accessible place and subject to examination by Commission staff; (vii) the net asset value per share with respect to unregistered money market fund shares is determined by dividing the value of the assets belonging to the fund, less the liabilities of the

Unregistered money market funds are typically organized by a fund adviser for the purposes of managing the cash of other funds in a fund complex and operate in almost all respects as a registered money market fund, except that their securities are privately offered and thus not registered under the Securities Act of 1933.<sup>50</sup> Although a fund's investments in unregistered money market funds is no longer restricted by section 12(d)(1),<sup>51</sup> these investments are subject to the affiliate transaction restrictions in the Act and rules thereunder and thus require exemptions from sections 17(a) and 17(d), and rule 17d-1.<sup>52</sup>

Under the proposed rule, the exemption would be available only for investments in an unregistered money market fund that operates like a money market fund registered under the Act.<sup>53</sup> To be eligible, an unregistered money market fund would be required to (i) limit its investments to those in which a money market fund may invest under

fund, by the number of outstanding shares of the fund; (viii) the acquiring fund purchase and redeem shares of the unregistered money market fund as of the same time and at the same price, and receive dividends and bear its proportionate share of expenses on the same basis, as other shareholders of the unregistered money market fund; and (ix) a separate account is established in the shareholder records of the unregistered money market fund for the account of the acquiring fund. These orders provide exemptions for funds with the same adviser as the unregistered money market funds. The proposed rule would permit funds to invest in unregistered money market funds with the same or a different adviser.

<sup>50</sup> See, e.g., Pioneer Application, *supra* note 37, conditions 7.<sup>8</sup> See also 15 U.S.C. 80a-3(c)(1) (excepting from the definition of "investment company" issuers whose securities are owned by no more than 100 persons and which is not making and does not presently propose to make a public offering of its securities); 15 U.S.C. 80a-3(c)(7) (excepting from the definition of "investment company" issuers whose securities are owned exclusively by "qualified purchasers" and which is not making and does not presently propose to make a public offering of its securities).

<sup>51</sup> Before 1996, a fund that was excepted from the definition of "investment company" by section 3(c)(1) of the Act (because its shares were held by fewer than 100 beneficial owners and was not making and did not propose to make a public offering of its securities) was nonetheless deemed to be an "investment company" for purposes of section 12(d)(1). In 1996, Congress narrowed this provision of section 3(c)(1) to make section 12(d)(1) limitations inapplicable to an investment by a registered fund in shares of a fund that is not registered with us in reliance on section 3(c)(1). See NSMIA, *supra* note 25 § 209(a). A parallel provision was incorporated into section 3(c)(7), which excepts from the definition of "investment company" funds whose outstanding securities are owned exclusively by "qualified purchasers" and that is not making and does not propose to make a public offering of its securities. See section 3(c)(7)(D) [15 U.S.C. 80a-3(c)(7)(D)]. See also 1992 Study, *supra* note 17, at 105-110.

<sup>52</sup> See discussion above in section II.A.1(a) of this Release.

<sup>53</sup> Proposed rule 12d1-1(c)(3)(ii).

<sup>43</sup> Some applicants have sought, and we have granted, broader exemptive relief permitting funds to invest in funds that are not part of the same group of investment companies in excess of the limitations of section 12(d)(1). See *infra* notes 73, 75. Under those orders, funds in which the applicants could invest include money market funds.

<sup>44</sup> See H.R. Rep. No. 622, *supra* note 18, at 43 ("The Committee intends the rulemaking and exemptive authority in new Section 12(d)(1)(f) to be used by the Commission so that the benefits of funds [of funds] are not limited only to investors in the largest fund complexes, but, in appropriate circumstances, are available to investors through a variety of different types and sizes of investment company complexes.").

<sup>45</sup> See 15 U.S.C. 80a-2(a)(3)(A), (B).

<sup>46</sup> See discussion above in section II.A.1(a). We note that rule 17a-7 provides an exemption for purchase and sale transactions between registered funds (or series of registered funds) that are affiliated and that meet certain conditions regardless of the nature of the funds' affiliation. 17 CFR 270.17a-7.

<sup>47</sup> Section 17(e) of the Act prohibits a first or second-tier affiliate of a registered fund that acts as