

We would, however, retain one of the conditions of our orders relating to fees. Under proposed rule 12d1-1, the acquiring fund either would not pay any sales load, distribution fees, or service fees on acquiring fund shares, or if it did, the acquiring fund's investment adviser would have to waive a sufficient amount of its advisory fee to offset the cost of the loads or distribution fees.⁶⁹ Rarely do institutional investors (such as an acquiring fund) pay sales loads or bear distribution expenses on an investment in a money market fund. Thus, a money market fund that charges a sales load or distribution fees to the acquiring fund may not be an appropriate investment for that fund.

Comment is requested on the proposed rule. Should we retain any of the other conditions of the exemptive orders? Should a fund be limited in the amount of assets it can invest in one or more money market funds? If so, what is the appropriate limit? Should the proposed rule require fund directors to make findings regarding duplicative fees? Do the sponsors, advisers, or directors of money market funds have any concerns about other funds making large investments in their money market funds? Should we include any restrictions on the ability of an acquiring fund to redeem shares of a money market fund that is not part of the same group of investment companies?⁷⁰ Should we restrict the ability of an acquiring fund to vote shares of a money market fund that is

that acquiring fund directors determine that fees for advisory services provided to the acquiring fund are in addition to and not duplicative of fees paid for advisory services provided to the acquired funds. In his testimony before the House Subcommittee considering amendments to section 12(d)(1), the Director of our Division of Investment Management explained that such a condition was unnecessary because "[t]he Commission would be able to use its authority under the Securities Act [of 1933] to * * * address the potential for excessive layering of advisory fees by requiring an acquiring fund to disclose in the prospectus fee table the cumulative advisory fees paid by the acquiring and acquired funds." *Hearing on H.R. 1495 Before the Subcomm. on Telecommunications and Finance of the House Comm. on Commerce*, 104th Cong., 1st Sess. 19 (1995) (statement of Barry P. Barbash, Director, Division of Investment Management, Securities & Exchange Commission). See also *Hearing on S. 1815 Before the Senate Comm. on Banking, Housing and Urban Affairs*, 104th Cong., 2d Sess. 38 (1996) (statement of Arthur Levitt, Jr. Chairman, Securities and Exchange Commission).

⁶⁹ Proposed rule 12d1-1(b)(1). The proposed rule refers to "administrative fees," which it would define as "any sales charge, as defined in rule 2830(b)(8) of the Conduct Rules of the NASD or service fee, as defined in rule 2830(b)(9) of the Conduct Rules of the NASD, charged in connection with the purchase, sale, or redemption of securities issued by a Money Market Fund."

⁷⁰ A fund relying on section 12(d)(1)(F) may not redeem more than 1 percent of an acquired fund's shares during any period of less than 30 days. 15 U.S.C. 80a-12(d)(1)(F).

not part of the same group of investment companies?⁷¹ Are there reasons to restrict the ability of an acquired money market fund itself to have a cash sweep arrangement?

Some funds considering a cash sweep arrangement may not have an investment policy that specifically addresses such an arrangement. Should we require funds to adopt a policy before investing in shares of a money market fund? Alternatively, should we interpret fund investment policies and restrictions that apply to investments in money market instruments as applying to investments in money market funds?

B. Rule 12d1-2: Affiliated Funds of Funds

As discussed above, section 12(d)(1)(G) permits a registered fund to acquire an unlimited amount of shares of registered open-end funds and UITs that are part of the same "group of investment companies" as the acquiring fund. Since 1996, when the section was added to the Act, we have issued exemptive orders for a variety of fund of funds arrangements that we concluded were consistent with the public interest and the protection of investors, but that did not conform to section 12(d)(1)(G) limits.⁷²

Proposed rule 12d1-2 would codify, and in some cases expand, three types of relief provided to affiliated funds of funds.⁷³ In each case, the proposed rule provides relief from section 12(d)(1)(G) limitations on investments an affiliated fund of funds can make in addition to shares of funds in the same group of

⁷¹ A fund relying on section 12(d)(1)(F) must vote shares of an acquired fund either by seeking instructions from its shareholders, or in the same proportion as the vote of all other shareholders of the acquired fund. 15 U.S.C. 80a-12(d)(1)(F) (referencing 15 U.S.C. 80a-12(d)(1)(E)).

⁷² See, e.g., Scudder Kemper Investments, Inc., Investment Company Act Release No. 23691 (Feb. 11, 1999) [64 FR 8153 (Feb. 18, 1999)] (notice), Investment Company Act Release No. 23731 (Mar. 8, 1999) (order) (permitting a fund to invest in funds in the same group of investment companies and in limited amounts of funds in different fund companies); Nations Fund Trust, Investment Company Act Release No. 24781 (Dec. 1, 2000) [65 FR 77050 (Dec. 8, 2000)] (notice), Investment Company Act Release No. 24804 (Dec. 27, 2000) (order) (permitting a fund to invest in funds in the same group of investment companies and in other securities (not issued by another fund)).

⁷³ We are not at this time proposing to codify the broader relief we have granted to permit an affiliated fund of funds to acquire shares of funds in different groups of investment companies in excess of the limits of section 12(d)(1)(F). See Nationwide Life Insurance Co., Investment Company Act Release No. 25492 (Mar. 21, 2002) [67 FR 14735 (Mar. 27, 2002)] (notice), Investment Company Act Release No. 25528 (Apr. 16, 2002) (order); Schwab Capital Trust, Investment Company Act Release No. 24067 (Oct. 1, 1999) [64 FR 54939 (Oct. 8, 1999)] (notice), Investment Company Act Release No. 24113 (Oct. 27, 1999) (order).

investment companies. The other limitations in section 12(d)(1)(G) would continue to apply to a fund of funds relying on that provision.⁷⁴

1. Investments in Unaffiliated Funds

Section 12(d)(1)(G) permits a fund to acquire only funds that are part of the same group of investment companies. We propose to permit an affiliated fund of funds also to acquire up to three percent of the securities of funds that are not part of the same group of investment companies, subject to the limits in section 12(d)(1)(A) or 12(d)(1)(F).⁷⁵ This exemption would, in effect, permit funds to combine the relief provided by the statutory exceptions.⁷⁶ There do not appear to be any greater risks to an acquired fund or its shareholders if three percent of its shares are acquired by an affiliated fund of funds as opposed to being acquired by other types of mutual funds specifically permitted to purchase the shares by section 12(d)(1)(A) or 12(d)(1)(F). We seek comment on the proposed exemption. Are there greater risks to an acquired fund if the investor in these circumstances is an affiliated fund of funds?

2. Investments in Other Types of Issuers

To restrict the use of the exemption provided by section 12(d)(1)(G) to a "bona fide" fund of funds, Congress

⁷⁴ See *supra* notes 28-29, and accompanying text.

⁷⁵ Proposed rule 12d1-2(a)(1). A fund relying on section 12(d)(1)(A) (together with any companies or funds it controls) could not acquire more than 3 percent of the securities of any other fund in a different fund group. In addition, the acquiring fund would be limited to investing no more than 5 percent of its own assets (together with assets of any companies it controls) in the securities of any one fund in a different fund group, and no more than 10 percent of its assets (together with assets of any companies it controls) in securities of other funds in one or more different fund groups, in the aggregate. See 15 U.S.C. 80a-12(d)(1)(A)(i)-(iii). A fund relying on section 12(d)(1)(F) (together with its affiliates), could not acquire more than 3 percent of the securities of any other fund in a different fund group. The acquiring fund also would be required either to seek instructions from its shareholders as to how to vote shares of those acquired funds, or to vote the shares in the same proportion as the vote of all other shareholders of the acquired fund. See 15 U.S.C. 80a-12(d)(1)(F) (referencing 15 U.S.C. 80a-12(d)(1)(E)). In addition, the acquiring fund would be limited to charging a sales load of 1½ percent on its shares and would be prevented from redeeming more than 1 percent of the shares of any acquired fund during any period of less than 30 days. *Id.*

⁷⁶ We have issued a number of exemptive orders granting similar relief. See, e.g., Sage Life Assurance of America, Inc., Investment Company Act Release No. 25098 (Aug. 1, 2001) [66 FR 41272 (Aug. 7, 2001)] (notice), Investment Company Act Release No. 25142 (Aug. 28, 2001) (order); Scudder Kemper Investments, Inc., Investment Company Act Release No. 23691 (Feb. 11, 1999) [64 FR 8153 (Feb. 18, 1999)] (notice), Investment Company Act Release No. 23731 (Mar. 8, 1999) (order).