

- We request comment on whether the circumstances involving single subadvisers are sufficiently similar to those involving multiple subadvisers, to justify similar treatment under the proposed amendments.
- Should the proposed rule include as a condition that the principal adviser engage multiple subadvisers for each fund, or each series of the fund? Should any of the conditions in the rule be modified in the case of single subadviser funds?

B. Rescission of Previously Issued Exemptive Orders

As discussed above, we have issued over 100 orders permitting manager of managers funds to operate without the need for shareholder approval of new subadvisory contracts. Our rule proposal today is designed largely to codify the relief we have provided by order. However, the conditions in some of the orders vary slightly from others.⁵⁰ We are concerned that, if we permit the continued operation of funds under the orders we have issued in the past, funds will be operating under different sets of conditions, which might have an adverse effect on competition.⁵¹ We therefore anticipate rescinding those orders upon adoption of the proposed rule.

- We request comment on the possible effects caused by the rescission of the orders. If the Commission does not rescind the orders, how would competition be affected?

III. General Request for Comment

The Commission requests comment on the proposed rule, rule amendments, and form amendments proposed in this Release. The Commission also requests suggestions for additional changes to existing rules or forms, and comments on other matters that might have an effect on the proposals contained in this Release. Commenters are requested to provide empirical data to support their views.

IV. Cost-Benefit Analysis

The Commission is sensitive to the costs and benefits imposed by its rules.

exemptive relief. See Hillview Investment Trust II and Hillview Capital Advisors, LLC, Investment Company Act Release No. 25055 (June 29, 2001) [66 FR 35676 (July 6, 2001)].

⁵⁰ It is not unusual for the conditions in our orders to evolve as we and our staff gain experience with the operation of a type of a fund under an exemptive order.

⁵¹ The rescission of the orders would not affect existing subadvisory contracts entered into under an order prior to the adoption of the proposed rule. However, new or renewed subadvisory contracts entered into after adoption of the proposed rule would have to comply with the proposed rule's requirements.

As discussed above, proposed rule 15a-5 and the proposed amendments to Form N-1A would essentially codify existing exemptive orders that allow manager of managers funds and their principal advisers to enter into subadvisory contracts without shareholder approval. Therefore this analysis examines the costs and benefits to funds, advisers, and investors that would result from reliance on the exemptive relief under the proposed amendments, in comparison to the costs and benefits associated with obtaining an exemptive order from the Commission.

A. Benefits

We anticipate that funds, their advisers, and their shareholders would benefit from the proposed rule and amendments.⁵² Funds and advisers that rely on the rule would be able to enter into subadvisory contracts without obtaining exemptive relief from the Act's shareholder approval requirement, which relief can be costly to funds and their shareholders.⁵³ Obtaining an exemptive order also can entail delays for the fund that applies for relief, although these applications for relief are typically processed expeditiously.⁵⁴

Some of the conditions included in the proposed rule and amendments differ from the conditions or representations typically included in a manager of managers exemptive order. We anticipate that these differences will not yield significant costs or benefits. For example, an exemptive order for a fund that intends to provide only aggregate fee disclosure concerning subadvisers typically requires that the fund's independent directors retain independent legal counsel.⁵⁵ The proposed rule would not require

⁵² Our staff estimates that approximately 2,798 portfolios (comprising portions of 631 open-end funds) have at least one subadviser and as such could benefit from the proposed rule and amendments. The staff's estimates are based on an examination of the information reported on Form N-SAR from July through December 2002.

⁵³ Based on discussions with fund representatives, the Commission estimates that obtaining an exemptive order for a manager of managers fund costs approximately \$35,000.

⁵⁴ Our staff estimates, based upon orders issued in the past, that the exemptive application process (from initial filing to issuance of order) takes about eight months. During that time, Commission staff review and comment on applications, applicants submit responses to comments, the completed application is summarized in a notice to the public, and public comments are received and evaluated.

⁵⁵ See, e.g., Pitcairn Funds and Pitcairn Trust Company, Investment Company Act Release Nos. 25106 (Aug. 9, 2001) [66 FR 42901 (Aug. 15, 2001)] (notice) and 25150 (Sept. 5, 2001) [75 SEC Docket 2214 (Oct. 2, 2001)] (order).

independent directors to retain legal counsel.

B. Costs

Funds that choose to rely on the proposed amendments, as well as their advisers, would incur certain costs in complying with the rules.⁵⁶ As discussed above, proposed rule 15a-5 includes a condition requiring the contract between a manager of managers fund and its principal adviser to provide that the adviser will supervise and monitor the performance of its subadvisers.⁵⁷ If the Commission rescinds the previous exemptive orders granted for manager of managers funds, a fund that already has an exemptive order would need to modify its advisory contract to include that provision. Similarly, if an existing fund were to choose to operate as a manager of managers fund under the proposed amendments, it would need to modify its advisory contract.⁵⁸

The modification of advisory contracts in response to the proposed rule would impose one-time costs. The Commission anticipates providing a sufficiently long compliance period for the proposed amendments, so that the contract modifications could be made when the fund's board next approves a new advisory contract. Therefore we believe the costs involved in making the modifications would be minor.⁵⁹

There are no new costs associated with any of the remaining conditions of the proposed rule and amendments. First, the proposed rule would require that the fund provide shareholders,

⁵⁶ Because the proposed rule is an exemptive rule, funds can choose whether or not to rely on it. Only those funds that choose to rely on the proposed rule would incur costs in complying with the rule.

⁵⁷ See *supra* Section II.A.2.

⁵⁸ Under our proposal, contracts between the principal adviser and subadvisers also would be required to authorize the principal adviser to terminate the subadvisory contract at any time without penalty. However, most if not all subadvisory contracts already contain such a provision, and therefore this condition would not impose a new cost on funds.

⁵⁹ For purposes of the Paperwork Reduction Act, the Commission staff has estimated that it would take a total of 5 hours and \$1,287.77 per fund to comply with the condition of proposed rule 15a-5 related to the supervision of subadvisers. During the first year after adoption of the rule, it is estimated that all funds that currently rely on exemptive orders (plus existing funds that would choose to rely on the proposed rule during the first year) would spend a total of 600 hours and \$154,719 to comply with the supervision requirement. After the first year, the staff estimates that ten funds per year, whose securities have already been publicly offered, would seek to rely on the proposed rule and therefore would need to modify their advisory contracts with principal advisers. The Commission staff estimates that, after the first year, those ten funds together would annually spend 50 hours and \$12,877 to comply with the supervision requirement.