

Introducing Broker from the Clearing Broker could be deemed a prohibited transaction. In this regard, the decision by GSL, acting as a fiduciary of a Client Plan, to lend such securities to the Clearing Broker could be deemed to violate section 406(b) of the Act. Accordingly, the Applicants have requested relief from section 406(a), 406(b)(1), 406(b)(2), and 406(b)(3) of the Act and section 4975(c)(1)(A) through (F) of the Code for the receipt of such compensation paid to the Introducing Broker by the Clearing Broker; provided that certain conditions are satisfied.

The Applicants have also requested that the underlined phrase, below, from the opening paragraph of PTE 97-63, be deleted from the proposed exemption:

The restrictions of sections 406(a)(1)(A) through (D) and 406(b)(1) and (b)(2) of the Act and the sanctions resulting from the application of section 4975 of the Code, by reason of section 4975(c)(1)(A) through (E) of the Code, shall not apply to the lending of securities to State Street Bank and Trust Company (State Street), acting through its Financial Markets Group (FMG) (formerly the Money Market Division of the Capital Markets Area) or acting through any other division or U.S. affiliate of State Street that is a successor to the activities of FMG; and shall not apply to the lending of securities to any U.S. registered broker-dealers affiliated with State Street (the Affiliated Broker Dealers) by employee benefit plans (the Client Plans or the Client Plan), including commingled investment funds holding plan assets *for which State Street, through its Master Trust Services Division (the Trust Division) acts as directed trustee or custodian, and for which State Street, through its Global Securities Lending Division or any other similar division of State Street or U.S. affiliate of State Street or of its parent (collectively, GSL) acts as securities lending agent (or sub-agent); and shall not apply to the receipt of compensation by GSL in connection with the transactions, provided that the following conditions are met.*

In this regard, the Applicants have informed the Department that State Street, in most cases, will be either the trustee or the custodian of the Client Plans. However, on occasion GSL may be retained as a securities lending agent by a Client Plan as to which State Street is neither the trustee nor the custodian. The Applicants do not believe that there is any reason to deprive such Client Plans of the opportunity to participate in securities lending transactions for which GSL acts as agent (or sub-agent). Further, the Applicants do not believe that there is any reason to impose the incremental administrative burdens on GSL that would be entailed, if such Client Plans were treated differently from all other securities lending clients in this regard. Accordingly, the Applicants request that the specified

phrase in PTE 97-63 not be included in the language of the proposed exemption in order to provide the flexibility needed to enable a non-trustee, non-custodial Client Plan to lend securities.

In connection with the expansion of PTE 97-63, the Applicants have requested relief which would permit securities lending by certain index funds (the Index Fund(s)) or model-driven funds (the Model-Driven Fund(s)) managed by State Street or one of its divisions or U.S. affiliates. Specifically, the Applicants request that the Department modify Condition (a) of PTE 97-63. In this regard, Condition (a) of PTE 97-63 precludes the lending of securities to the SSB Group, if State Street or any of its divisions or affiliates has or exercises discretionary authority or renders investment advice with respect to the assets being lent. The Applicants have acknowledged that section II(a) in this proposed exemption precludes the lending of securities to either the SSB Group or the Clearing Broker, if State Street, the Clearing Broker, or any affiliate of State Street or the Clearing Broker has discretionary authority or renders investment advice with respect to such securities.

However, the Applicants note that the management of Index Funds and Model-Driven Funds entails a very limited degree of discretionary authority. As a result, the Applicants maintain that the potential for the abuse which Condition (a), as set forth in PTE 97-63, was designed to protect against (*i.e.*, that the investment decisions relating to a portfolio will be influenced by the possibility that the securities in such portfolio will be available for loan to an affiliated borrower) is not present in the context of Index Funds and Model-Driven Funds. Accordingly, the Applicants have requested that the language of section II(a) of this proposed exemption permit the lending of securities by an Index Fund or a Model-Driven Fund, managed by State Street or one of its divisions or U.S. affiliates, to members of the SSB Group or to the Clearing Broker. In this regard, the Applicants submit that it would be in the interest of such Index Funds and Model-Driven Funds to allow such funds to lend securities, as this would increase the securities lending opportunities available to such funds and enable such funds to generate additional securities lending revenue.

In addition, the Applicants request that the proposed exemption incorporate various modifications to specific terms and conditions, as set forth in PTE 97-63, including the following:

1. Modification of the language of Condition (f), as set forth in PTE 97-63, such that any reference to PTE 81-6 and PTE 82-63 also refer to such class exemptions as they may be amended from time to time or, alternatively, refer to any superseding class exemption that may be issued to cover securities lending by employee benefit plans. The Applicants maintain that the request is consistent with the Department's approach taken in Condition (d) of PTE 97-63 with respect to eligible collateral for securities loans.

2. Modification of the language in Condition (g), as set forth in PTE 97-63, to clarify that State Street is not required to indemnify the Client Plans against any potential investment losses associated with the investment of cash collateral received by such Client Plan in connection with securities lending transactions. The Applicants maintain that the request incorporates language previously provided by the Department in an interpretive letter relating to PTE 97-63.⁴

3. Change in the language of Condition (j), as set forth in PTE 97-63, to modify the plan size requirement in a context of master trusts and collective investment funds. In this regard, Condition (j), as set forth in PTE 97-63, provides that only Client Plans with total assets having an aggregate market value of at least \$50 million are permitted to lend securities to the SSB Group. The Applicants note that in recent years the Department, in various class exemptions and individual exemptions, has recognized that the plan size requirement should be adjusted in the case of two or more Client Plans whose assets are commingled for investment purposes in a master trust or collective fund, provided certain conditions are satisfied. Accordingly, the Applicants request that the language in section II(j) of this proposed exemption address master trusts and collective funds in a comparable manner. It is represented that the specific language suggested by the Applicants for this purpose is substantially similar to that found in Prohibited Transaction Exemption 2002-45 (PTE 2002-45) granted to Deutsche Bank AG, as amended.⁵

(4) Modification of the language of Condition (l), as set forth in PTE 97-63, to require quarterly, rather than

⁴ Letter from Ivan L. Strasfeld, Director, Office of Exemption Determinations, U.S. Department of Labor, to William A. Schmidt, Esq. and Eric Berger, Esq. (February 27, 2001) (C-9199).

⁵ PTE 2002-45; granted (67 FR 59564, September 23, 2002, as corrected, 67 FR 69046, November 14, 2002); proposed (67 FR 9070, February 27, 2002); application no. D-10924.