

MEMO# 13671

June 22, 2001

SEC ISSUES NO-ACTION LETTER ON 401(K) INVESTMENTS

[13671] June 22, 2001 TO: PENSION COMMITTEE No. 38-01 RE: SEC ISSUES NO-ACTION LETTER ON 401(K) INVESTMENTS The Division of Investment Management of the Securities and Exchange Commission recently issued a no-action letter regarding when 401(k) plans may invest in private investment companies excepted from registration under Section 3(c)(7) of the Investment Company Act of 1940. 401(k)s may invest in such companies as long as plan participants are allowed to make investment decisions only from among "generic investment objectives," without being able to make individual decisions about investment in the Section 3(c)(7) fund. In these instances, the 401(k) plan would be considered to be the qualified purchaser for purposes of Section 3(c)(7) and not the plan participants. The facts of the no-action letter are as follows. H.E. Butt Investment and Retirement Plan, a defined contribution plan, offers participants six investment options: an aggressive fund, a general fund, a conservative fund, a stocks-only fund a bonds-only fund and a money market fund. Participants may choose from among these investment options, but the investment decisions for each of these investment options is made by an investment committee made up of five of the eight plan trustees. The plan has invested portions of the aggressive fund and the general fund in private investment companies excepted from registration under Section 3(c)(1). The plan follows the representations set out in the 1995 Standish Ayer no-action letter. The plan asks whether it would be possible to follow similar representations in investing in Section 3(c)(7) funds. The staff stated its position regarding counting plan participants when determining investors in Section 3(c)(1) in two prior no-action letters. In the 1993 PanAgora letter, the staff found that when plan participants may direct an investment in a particular Section 3(c)(1) fund, each one of them should count as an individual investor for the purpose of determining compliance with the 100-person limit for investing in a Section 3(c)(1) fund. In Standish Ayer, the staff stated that a retirement plan that offers only generic investment options should be treated as a single beneficial owner of the Section 3(c)(1) fund's securities. When it adopted rules to implement Section 3(c)(7), which was enacted as part of the National Securities Markets Improvement Act of 1996, the Commission questioned whether the position taken in Standish Ayer was consistent with that taken in PanAgora for the purposes of Section 3(c)(1) and whether Standish Ayer was appropriate in the context of Section 3(c)(7). 2The staff has affirmed that the positions taken in PanAgora and Standish Ayer are consistent and that Standish Ayer is appropriate for purposes of Section 3(c)(7). Therefore, the H.E. Butt Plan may be considered the qualified purchaser for the purposes of investing in Section 3(c)(7) funds subject to the representations it made in its letter, including:

- Other than plan trustees acting in their capacity as plan fiduciaries, a plan participant's investment discretion will be limited to allocating his or her account among a number of investment options, each of which has an identified investment objective.
- The decision to invest the

asset of an investment option in a Section 3(c)(7) fund, to withdraw the investment and the amount of assets invested will be made only by plan fiduciaries. • At least 50% of the assets of an investment option will consist of assets other than Section 3(c)(7) funds. • The plan will not make any representations to participants concerning investments in Section 3(c)(7) funds. Any communication to participants that mentions such an investment will contain a disclaimer that there is no assurance that the investment option will continue to invest its assets, or the same portion of its assets, in the Section 3(c)(7) fund. A copy of the H.E. Butt no-action letter is attached. Kathryn A. Ricard Associate Counsel Attachment Attachment (in .pdf format)

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