

MEMO# 15097

September 4, 2002

INSTITUTE FILES SUPPLEMENTAL COMMENT LETTER ON PROPOSED AMENDMENTS TO RULE 17F-4

[15097] September 4, 2002 TO: CLOSED-END INVESTMENT COMPANY COMMITTEE No. 35-02 COMPLIANCE ADVISORY COMMITTEE No. 72-02 SEC RULES COMMITTEE No. 69-02 RE: INSTITUTE FILES SUPPLEMENTAL COMMENT LETTER ON PROPOSED AMENDMENTS TO RULE 17f-4 As we previously informed you, the Securities and Exchange Commission issued a proposal to amend Rule 17f-4 under the Investment Company Act of 1940, the rule that relates to custody of investment company assets with a securities depository.¹ The Institute commented on the proposed rule amendments earlier this year.² The Association of Global Custodians submitted a supplemental comment letter on the proposed amendments raising, among other things, the appropriateness of the Commission amending Rule 17f-4 to subject fund custodians to minimum performance standards in discharging their duties under UCC Article 8 with respect to custodied fund securities that are held indirectly through securities depositories.³ The Institute has filed the attached comment letter further stating its views on this issue. The Institute's letter states that it is necessary and appropriate for the Commission to subject fund custodians to minimum performance standards. The letter notes that the Institute's recommended "due care" performance standard is the same as the standard that automatically applies to custodians under Article 8 unless contrary or more specific standards are imposed on them by contract or other law or regulation. The letter further notes that the Institute is not aware of (and the AGC letter does not reference) any other law or regulation that imposes contrary or more specific standards on custodians. Therefore, the effect of the recommended standard would simply be to preclude funds from establishing contractual

1 Memorandum to Closed-End Investment Company Committee No. 22-01, Compliance Advisory Committee No. 60-01, SEC Rules Committee No. 95-01, Transfer Agent Advisory Committee No. 95-01, Unit Investment Trust Committee No. 27-01, dated November 26, 2001. 2 See Memorandum to Closed-End Investment Company Committee No. 8-02, Compliance Advisory Committee No. 12-02, SEC Rules Committee No. 15-02, Transfer Agent Advisory Committee No. 9-02, Unit Investment Trust Committee No. 6-02, dated February 5, 2002. 3 That letter is available on the Commission's website at <http://www.sec.gov/rules/proposed/s72201/goelzer2.htm>. 2 performance standards for their custodians that are less stringent than the "due care" standard called for under Article 8. The letter recommends that the Commission amend Rule 17f-4 to require that a fund's contract with its custodian include a minimum standard of care. Specifically, according to the Institute's letter, the contract should provide that the custodian is obligated to exercise due care in accordance with reasonable commercial standards in discharging its duty as a securities intermediary to obtain and thereafter maintain financial assets corresponding to the security entitlements that the custodian

establishes for the fund. Dorothy M. Donohue Associate Counsel Attachment (in .pdf format)

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