

MEMO# 3973

August 3, 1992

INSTITUTE COMMENTS ON NASAA TWO-TIER FUND PROPOSAL

August 3, 1992 TO: SEC RULES COMMITTEE NO. 53-92 STATE LIAISON COMMITTEE NO. 28-92 INSTITUTIONAL FUNDS COMMITTEE NO. 16-92 RE: INSTITUTE COMMENTS ON NASAA TWO-TIER FUND PROPOSAL _____ As we previously advised you, the NASAA Investment Company Registration/Trading Practices Committee issued "Proposed Guidelines for the Registration of Master Fund/Feeder Funds" ("Portfolio/First-Tier Fund") ("proposed guidelines") for public comment in mid-June. The proposed guidelines would require narrative disclosure following the fee table which summarizes the expenses of the the Portfolio and first-tier fund ("FTF"). The proposed guidelines also set forth certain areas where additional disclosure may be appropriate in an FTF prospectus. (See Memorandum to SEC Rules Committee No. 41-92, State Liaison Committee No. 22-92 and Institutional Funds Committee No. 12-92, dated June 15, 1992.) The Institute submitted the attached comment letter to the NASAA Committee on the proposed guidelines. Initially, the Institute recognized the cooperative effort between the NASAA Committee and the SEC and noted that this dialogue should serve as a model for future issues involving both state and federal regulators. The Institute also applauded the regulatory approach taken by the NASAA Committee, i.e., identifying areas unique to the two-tier fund structure which may require additional disclosure rather than requiring specific language to be included in the FTF's prospectus. Moreover, the Institute specifically recommended that the NASAA Committee delete the proposal requiring thirty days advance written notice to shareholders if the investment objective of the Portfolio or FTF is changed and such occurs without a shareholder vote (i.e., the fund has a non-fundamental investment objective) since this is a general mutual fund issue and not one unique to two-tier funds. In addition, the Institute questioned why NASAA would require shareholder approval for conversion to a two-tier structure if such approval would not be required in order to convert under the provisions of the Investment Company Act of 1940 or applicable state corporate law. The Institute also objected to the proposed guideline which would have required disclosure informing investors "how" to obtain information about whether other FTFs in the same Portfolio are available to investors. The Institute strongly objected to the requirement which would require that the disinterested directors/trustees of the FTF may not be the same as the directors/trustees of the Portfolio -- in essence, requiring two separate boards. The Institute noted that although certain two-tier funds have elected to have separate boards for both the Portfolio and the FTF, such should not be mandated by the states. Moreover, separate boards are not required for affiliated funds in the same fund group, nor are they required for multi-class funds. A copy of the Institute's comment letter is attached. Members of NASAA will consider and vote on whether to adopt the proposed guidelines at the NASAA Fall Conference in September. If adopted by NASAA, it is

anticipated that the individual states will begin applying the disclosure requirements in the proposed guidelines sixty days after approval by NASAA members. We will keep you advised of developments. Patricia Louie Assistant Counsel Attachment

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