Investment Management Industry News Summary - August 2010

AUGUST 31, 2010

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View previous month...

SEC Adopts New Stockholder Proxy Access Rule Applicable to Public Companies, including Registered Investment Companies

August 25, 2010 12:03 PM

On August 25, 2010, the SEC adopted a new stockholder proxy access rule applicable to public companies. Notwithstanding significant industry comment opposing application of the proposed rule to registered investment companies, the SEC concluded that "facilitating the exercise of traditional state law rights to nominate and elect directors is as much of a concern for investment company shareholders as it is for shareholders of non-investment companies." The SEC articulated three reasons why it believed the costs of compliance with the rule for investment companies will be less than the costs for other companies:

First, to the extent investment companies do not hold annual meetings as permitted by state law, investment company shareholders will have less opportunity to use the rule.

Second,…the disproportionately large and generally passive retail shareholder base of investment

companies will probably mean that the rule will be used less frequently than will be the case with non-investment companies.

Third, because we have …[limited] use of…[the rule] to shareholders who have maintained significant continuous holdings in the company for at least three years, and because many funds, such as money market funds, are held by shareholders on a short-term basis, we believe that the situations where shareholders will meet the eligibility requirements will be limited.

For more information about the new rule, see the SEC Press Release, the SEC Adopting Release and "WilmerHale Legal Insights, SEC to Require Stockholder Proxy Access," dated August 25, 2010, available at:

http://www.sec.gov/news/press/2010/2010-155.htm

http://www.sec.gov/rules/final/2010/33-9136.pdf

http://www.wilmerhale.com/publications/whPubsDetail.aspx?publication=9592

transaction or matter addressed herein.

SEC Staff Grants No-Action Relief to Company Seeking to Rely on Section 3(c)(5) Exception from Definition of "Investment Company"

August 19, 2010 12:11 PM

On August 19, 2010, the SEC's Division of Investment Management granted no-action relief to a company that was primarily engaged in purchasing royalty interests obligating third parties to pay royalties to the company attributable to part of the sales price of biopharmaceutical products and was seeking to rely on the Section 3(c)(5) exception from the definition of investment company under the Investment Company Act. The Section 3(c)(5) exception is available to "[a]ny person who is not engaged in the business of issuing redeemable securities, face-amount certificates of the installment type or periodic payment plan certificates, and who is primarily engaged in [among other things]…[p]urchasing or otherwise acquiring … open accounts receivable, and other obligations representing part or all of the sales price of merchandise, insurance, and services." The company argued successfully, among other things, that the royalty interests at issue were similar to account receivables, which are specifically enumerated "obligations representing part or all of the sales price of merchandise" as set forth in Section 3(c)(5).

For more information, please see:

http://www.sec.gov/divisions/investment/noaction/2010/royaltypharma081310-7.pdf

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SEC Staff Provides No-Action Relief Delaying Designation of NRSROs by Money Market Fund Boards

August 19, 2010 12:07 PM

Under amendments to Rule 2a-7 under the Investment Company Act of 1940, as amended (the "Investment Company Act"), adopted by the SEC in February 2010, (1) each money market fund's board of directors was required to designate at least four nationally recognized statistical rating organizations ("NRSROs") for use by the fund to satisfy minimum ratings requirements, and (2) the fund was required to disclose such designations in its statement of additional information. On August 19, 2010, the SEC's Division of Investment Management released a no-action letter providing assurance that enforcement action will not be taken if the NRSRO designation and related disclosure are delayed until the SEC has completed its review of Rule 2a-7 as required by the Dodd-Frank Wall Street Reform and Consumer Protection and amended Rule 2a-7 accordingly. Until such amendment of Rule 2a-7, money market funds seeking to rely on this no-action relief must continue to comply with the obligations for determining and monitoring eligible securities set forth in Rule 2a-7 as previously in effect, except with respect to the limitation on holding unrated asset-backed securities repealed by the SEC's amendments to Rule 2a-7.

For more information, please see:

http://www.sec.gov/divisions/investment/noaction/2010/ici-nrsro081910.htm

For more information on the February 2010 amendments to Rule 2a-7, please see:

http://www.sec.gov/rules/final/2010/ic-29132.pdf

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NFA Files Rulemaking Petition with CFTC to Limit Registered Investment Company Exclusion from Definition of Commodity Pool Operator

August 18, 2010 12:14 PM

On August 18, 2010, the NFA submitted a rulemaking petition to the Commodity Futures Trading Commission ("CFTC") seeking to amend CFTC Regulation 4.5, which currently provides an exclusion from the definition of commodity pool operator ("CPO") for registered investment companies, subject to the filing of a notice with the NFA. Under the rule amendment sought by the NFA, a registered investment company would only qualify for exclusion from the definition of CPO, if (1) it does not market interests to the public as interests in a commodity pool or in a vehicle to gain exposure to commodity futures or options, and (2) it uses commodity futures or options solely (a) for bona fide hedging purposes and (b) for positions that are not for non-bona fide hedging purposes, only to the extent that the aggregate initial margin and premiums necessary to establish the positions are limited to 5% of the liquidation value of its portfolio. In other words, the NFA is seeking to revert to the pre-2003 provisions of Regulation 4.5.

The petition recognizes that adoption of the rule amendment would mean that a number of registered investment companies currently operating in reliance on the CPO exclusion may no longer be eligible for that exclusion. Accordingly, it encouraged the CFTC to provide adequate time for these funds to comply with any amended regulation.

In order for the proposal to move forward, the CFTC would have to publish the proposed amendment in the Federal Register and provide an opportunity for public comment.

For more information, please see:

http://www.nfa.futures.org/news/newsPetition.asp?ArticleID=3630

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SEC Director of Division of Investment Management to Leave SEC

August 17, 2010 12:01 PM

On August 17, 2010, the SEC announced that the Director of the Division of Investment Management, Andrew J. “Buddy” Donohue, will be leaving the SEC in November of this year. As noted in the SEC press release, during his tenure, the SEC adopted rules to improve oversight of money market funds, increase investment adviser custody controls, and curtail investment adviser "pay-to-play" abuses; proposed rules to reform Rule 12b-1 mutual fund distribution fees and revise information in target date fund advertisements and marketing; and implemented the new mutual fund summary prospectus and investment adviser disclosure brochure.

For more information, please see:

http://www.sec.gov/news/press/2010/2010-151.htm

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Ninth Circuit Holds No Private Right of Action under Section 13(a) of the Investment Company Act

August 12, 2010 12:17 PM

On August 12, 2010, the U.S. Court of Appeals for the Ninth Circuit, overturned a decision of the District Court of the Northern District of California by holding that Section 13(a) of the Investment Company Act does not create a private cause of action or recognize that such a private cause of action exists. Section 13(a) of the Investment Company Act prohibits registered investment companies from changing certain investment policies as set forth in their registration statements unless they have obtained prior shareholder approval.

In the case, mutual fund investors claimed that the fund deviated from the investment policies described in its registration statement to the detriment of the fund's investors in violation of Section 13(a). The District Court had held that a private cause of action was implied in Section 13, relying

on, among other things, the addition of Section 13(c) to the Investment Company Act pursuant to the Sudan Accountability and Divestment Act of 2007 ("SADA"). Section 13(c) prohibits any remedy or cause of action relating to a registered investment company's failure to invest in or divestment from investments in certain specified industrial sectors of Sudan. The District Court concluded that Congress would have no basis to bar actions based on Sudanese divestments if Section 13 did not authorize private causes of action. However, in overturning the District Court's decision, the Ninth Circuit reasoned, among other things, that Congress could not have intended to restrict the application of Section 13(c) solely to causes of action arising from divestments that might otherwise violate Section 13(a), because the legislative history of SADA demonstrated that Section 13(c) barred actions for a broader range of violations; not just violations of Section 13. Moreover, the appellate court noted that Congress's recent amendment of Section 13(c)(2)(A) expressly states that Section 13(c)(1) "does not create or affect the existence of a private right of action under Section 13(a)."

For more information, please see:

http://www.ca9.uscourts.gov/datastore/opinions/2010/08/12/09-16347.pdf

(ii) promoting, marketing or recommending to another party any transaction or matter addressed herein.

SEC Approves Final Rule Delegating Authority to Issue Formal Orders of Investigation

August 11, 2010 2:40 PM

On August 11th, the SEC approved a rule amendment to extend the delegation of authority to issue formal orders of investigation. In August of 2009, the SEC delegated this authority to the Director of the Enforcement Division for a one-year period. The rule amendment adopted this week deletes the sunset provision and ensures that the Enforcement Director will retain the ability to authorize formal orders and extend subpoena powers to the staff without Commission oversight. According to the release, the SEC determined that extending this authorization was appropriate based on effective communication between the Division and the Commission to resolve legal and policy concerns surrounding formal orders and the increased efficiency with which the Division is able to pursue enforcement actions using the delegated authority.

For more information, please see:

http://www.knowledgemosaic.com/gateway/Rules/FR.34-62690.081110.pdf

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SEC Staff Provides Guidance Regarding Short-Term Floating Rate Securities Under Rule 2a-7

August 10, 2010 2:37 PM

On August 10th, the SEC staff published a letter clarifying the treatment of short-term floating rate securities under Rule 2a-7 of the Investment Company Act. The staff indicated that when calculating a money market fund's weighted average portfolio maturity under Rule 2a-7(c)(2)(iii), it is permissible to treat a short-term floating rate security that is subject to an unconditional demand feature as having a maturity equal to the period remaining until the principal can be recovered through demand. The staff was responding to concerns that the language of the rule unintentionally affords different treatment to variable and floating rate securities. On its face, the rule permits a money market fund to rely on the demand feature of a variable rate security when calculating its maturity, but only allows the fund to use the stated final maturity date for a short-term floating rate security, even if it had a shorter demand feature. The staff's interpretation released this week should enable money market funds to apply consistent treatment to floating and variable rate securities and determine maturity for each type of security based on unconditional demand features.

For more information, please see:

http://www.sec.gov/divisions/investment/noaction/2010/ici081010.htm

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