SUPPORTING STATEMENT
RULE 15a-5

A. JUSTIFICATION

1. Necessity for the Information Collection

A growing number of investment companies ("funds")[1] are now offered whose investment advisers do not directly manage a portfolio of securities. Instead, the advisers supervise one or more subadvisers,[2] which are themselves responsible for the day-to-day management of the funds' portfolios. In these "manager of managers" funds, the investment adviser seeks to achieve the funds' investment objectives by hiring, supervising and, when appropriate, discharging subadvisers, each of which is responsible for the management of a portion of a fund's portfolio.[3] In many cases, these funds also authorize the adviser to allocate and reallocate fund assets among subadvisers. Today more than 100 fund complexes offer these types of funds, which hold more than 400 billion dollars in assets.[4]

A number of manager of managers funds have obtained from the Commission exemptions from section 15(a) of the Investment Company Act of 1940 (15 U.S.C. 80a-15(a)) (the "Investment Company Act" or "Act"), which prohibits any person from serving as an

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[1] In this supporting statement, we use the term "fund" to mean a registered open-end management investment company or a separate series of such a company.

[2] In this supporting statement, we use the term "subadviser" to mean a party that contracts with a fund's principal adviser to provide investment advisory services to the fund, and the term "principal adviser" to mean a party that contracts directly with a fund to provide investment advisory services to the fund. *See* proposed rule 15a-5(b)(2) – (3) (17 CFR 270.15a-5(b)(2) - (3)) (defining "principal adviser" and "subadviser" by reference to sections 2(a)(20)(A) – (B) of the Act (15 U.S.C. 80a-2(a)(20)(A) – (B))).

[3] In the case of a series fund, the adviser seeks to achieve the fund's investment objectives by hiring, supervising and, when appropriate, discharging subadvisers for the management of all or a portion of the portfolio of a series.

[4] Since 1995 we have issued over 100 orders allowing manager of managers funds to retain subadvisers (and materially amend subadvisory contracts) without shareholder approval.

investment adviser (or a subadviser) to a fund except under a written contract that the fund's shareholders have approved.[5] Many sponsors of these funds have asserted that without relief from the shareholder voting requirement, the costs and delays associated with obtaining a shareholder vote would prevent advisers from hiring and firing subadvisers and from achieving the funds' investment objectives. They also have asserted that the underlying purpose of section 15(a)—to give shareholders a voice in the fund's investment advisory arrangements[6] — would be satisfied without a shareholder vote on the subadvisory contracts because the principal adviser's contract must still be approved by fund shareholders. Sponsors have analogized subadvisers in a manager of managers arrangement to portfolio managers employed by a fund adviser who may be hired and fired without the consent of shareholders.[7]

Proposed rule 15a-5 (17 CFR 270.15a-5) and amendments to Form N-1A (17 CFR 239.15A, 17 CFR 274.11A) together would codify the orders we have issued for manager of managers funds, including many of their conditions, allowing any fund that satisfies the conditions to enter into or materially amend a subadvisory contract without shareholder approval. To provide for the protection of fund shareholders, a fund that relied on the proposed rule would have to satisfy a number of conditions, some of which would result in information collection requirements. The proposed rule and amendments are designed to limit the scope of the relief to subadvisers of manager of managers funds, and to assure that investors in these

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[5] See supra note Error: Reference source not found.

[6] See Investment Trusts and Investment Companies: Hearings on S. 3580 Before the Subcomm. of the Senate Comm. on Banking and Currency, 76th Cong., 3d Sess. 253 (1940) (statement of David Schenker).

[7] See, e.g., TIFF Investment Program, Inc. and Foundation Advisers, Inc., Investment Company Act Release Nos. 21268 (Aug. 3, 1995) [60 FR 40875 (Aug. 10, 1995)] (notice) and 21328 (Aug. 30, 1995) [60 SEC Docket 316 (Sept. 26, 1995)] (order), in which the applicant had represented that the employment of a new subadviser was "closely analogous to the decision by a money management firm to hire another portfolio manager or analyst." See id., Investment Company Act Release No. 21268, at text following n.1.

funds are fully informed of the identity of the current subadviser(s) managing their portfolio and of the fact that subadvisers could be added or replaced without shareholder approval.

The collections of information required by proposed rule 15a-5 would be voluntary because rule 15a-5 is an exemptive rule and, therefore, funds may choose not to rely on the proposed rule. The proposed rule would require that all advisory and subadvisory contracts contain certain provisions. Specifically, all the fund's subadvisory contracts for which shareholder approval is not sought would have to provide the principal adviser with the authority to terminate the subadvisory contract at any time, on no more than 60 days written notice, without payment of penalty. In addition, the advisory contract between each principal adviser and the fund would have to require that the principal adviser supervise the activities of its subadvisers. These provisions are intended to ensure that only manager of managers funds (in which subadvisers resemble and perform the duties of a portfolio manager in a typical fund) are eligible for relief under the proposed rule and to allow the principal adviser to carry out its principal duties to the fund, the selection and monitoring of subadvisers, in an efficient manner.

The proposed rule also would require funds to provide shareholders (and file with the Commission) with an information statement within 90 days after entry into the subadvisory contract or after making a material change to a wholly-owned subsidiary's existing subadvisory contract. The information statement must describe the agreement and contain all of the information that shareholders would have received in a proxy statement had a shareholder vote been held. This information collection is needed to ensure that shareholders are aware of the identity of the subadvisers that would be making investment decisions for the fund and the terms of each subadvisory contract.

2. Purposes of the Information Collection

The purpose of the information collection requirements in proposed rule 15a-5 is to ensure that only manager of managers funds are eligible for relief under the proposed rule and that the interests of the fund and its shareholders are sufficiently considered and protected in situations in which the fund and its principal adviser(s) are permitted to enter into subadvisory contracts without shareholder approval. The information collections in the rule also ensure that shareholders are provided with information on the identity of the fund's subadvisers.

3. Role of Improved Information Technology

Proposed rule 15a-5 would require that funds relying on the rule file with the Commission the information statement sent to shareholders. The Commission's Electronic Data Gathering, Analysis and Retrieval system ("EDGAR") is designed to automate the filing, processing, and dissemination of full disclosure filings. The system permits publicly held companies to transmit their filings to the Commission directly over the Internet. This automation has increased the speed, accuracy, and public availability of information, generating benefits to investors and financial markets. The information statement would be required to be filed electronically with the Commission on EDGAR.[8] The public may access filings on EDGAR through the Commission's Internet web site (http://www.sec.gov) or at EDGAR terminals located at the Commission's public reference rooms.

[8] See 17 CFR 232.101(a)(1)(iii).

Proxy (or information) statements for funds may be sent to investors by electronic means so long as the fund meets certain requirements.[9] The Commission has no information concerning the percentage of such documents sent electronically, but believes it is a small percentage.

4. Efforts to Identify Duplication

The Commission is not aware of any duplicate reporting or recordkeeping requirements concerning proposed rule 15a-5.

5. Effects on Small Entities

Proposed rule 15a-5 would be available to all funds that use one or more subadvisers regardless of the size of the funds, as long as the funds and their principal advisers comply with the conditions set forth in the rule. Proposed rule 15a-5 would not disproportionately burden small entities. The risks accompanying the funds' use of subadvisers without shareholder approval would not vary based on the size of the entities involved.

6. Consequences of Less Frequent Collection

The information statement required by proposed rule 15a-5 would be given to shareholders only when subadvisers are retained without shareholder approval in reliance on the proposed rule. Because the Commission does not have control over the retention of subadvisers by funds, we cannot require less frequent collection unless we do not require the collection with respect to every subadviser that is retained by funds without shareholder approval pursuant to proposed rule 15a-5. Not requiring the disclosure of the information required by proposed rule 15a-5(a)(5) in an information statement would harm investors by denying them prompt

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[9] See Use of Electronic Media for Delivery Purposes, Investment Company Act Release No. 21399 (Oct. 6 1995) [60 FR 53458 (Oct. 13, 1995)].

information as to the identity of the fund's subadvisers responsible for investing a portion of the fund's assets.

Proposed rule 15a-5 also would require advisory and subadvisory contracts to contain certain terms. Advisory contracts between funds and principal advisers that use one or more subadvisers without shareholder approval pursuant to proposed rule 15a-5, would be required to obligate the principal adviser to supervise its subadvisers. Subadvisory contracts between principal advisers and those subadvisers would be required to be terminable at any time by the principal adviser, on no more than 60 days written notice, without payment of penalty. These information collection requirements would be one-time events.

7. Inconsistencies With Guidelines in 5 CFR 1320.5(d)(2)

Not applicable.

8. Consultations Outside the Agency

The Commission requested public comment on the collection of information requirements in rule 15a-5 before it submitted this request for extension and approval to the Office of Management and Budget. The Commission received no comments in response to its request.

9. Payment or Gift to Respondents

Not applicable.

10. Assurances of Confidentiality

Not applicable.

11. Sensitive Questions

Not applicable.

12. Estimate of Hour Burden

The estimate of the number of funds responding to the proposed rule is based on statistics compiled by the Commission from various sources. The burden hour estimates for responding to rule 15a-5 are based on consultations with fund representatives. The estimated average burden hours are made solely for purposes of the Paperwork Reduction Act and are not derived from a comprehensive or even representative study or survey of the cost of Commission rules.

The Commission staff estimates that 2961 portfolios (comprising portions of 614 registered open-end investment companies) currently use the services of one or more subadvisers and would be subject to the conditions contained in the proposed rule if they intend to retain subadvisers without shareholder approval.[10]

The proposed rule would require that a fund's contract with each principal adviser that retains the services of one or more subadvisers contain a provision obligating the principal adviser to supervise the activities of its subadvisers.[11] The proposed rule also would require all contracts with subadvisers that are retained without shareholder approval to provide that the principal adviser may terminate the subadviser at any time without penalty.[12]

During the first year after adoption of the rule, Commission staff estimates that each fund relying on the rule would incur an initial one-time burden to modify its existing contract with the principal adviser to require the principal adviser to supervise the activities of its subadvisers. Staff estimates this burden would be 5 hours per fund (4 hours by in-house counsel, 0.5 hours by

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[10] These estimates are based on an examination of information reported on Form N-SAR from September 2005 through February 2006.

[11] Proposed rule 15a-5(a)(4).

[12] Proposed rule 15a-5(b)(4). Most subadvisory contracts already contain terms that allow the principal adviser to terminate the contract at any time. We therefore estimate that there would be no burden hours or costs imposed on funds by this requirement.

fund directors, 0.5 hours by support staff).[13] Commission staff estimates that 149 funds would have to modify their advisory contracts with their principal advisers to comply with the proposed rule, which would result in an estimated total of 745 burden hours.[14] The total estimated first year cost of burden hours is $338,900[15] and 149 responses.

Commission staff estimates that after the first year, approximately 10 funds[16] would spend, on average, 5 hours annually (4 hours by in-house counsel, 0.5 hours by fund directors, 0.5 hours by support staff) to modify their advisory contracts with their principal advisers. Thus, the Commission estimates these modifications would result in a total of 50 burden hours. The total estimated annual cost of burden hours is $22,745[17] and 10 responses.

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13 These estimates are based on discussions with fund representatives.

14 These 149 funds include 125 funds that currently rely on exemptive orders, 14 funds that have filed an application for an exemptive order and, as explained infra note Error: Reference source not found, 10 additional funds that would choose to rely on the proposed rule during the first year. The total number of burden hours for the first year is 149 funds x 5 hours = 745 hours.

15 In calculating the first year total industry cost of complying with the contract modification (supervision) requirement, Commission staff estimated that 596 hours would be incurred by in-house counsel with a wage rate of $312 per hour (this figure), 74.5 hours incurred by fund directors with a wage rate of $2,000 per hour, and 74.5 hours incurred by clerical staff with an average wage rate of $53 per hour.

The wage rate for in-house counsel is from the SIA Report on Management & Professional Earnings in the Securities Industry 2005, and is modified to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead. The wage rate for clerical staff is from the SIA Report on Office Salaries in the Securities Industry 2005, and is modified to account for an 1800-hour work-year and multiplied by 2.93 to account for bonuses, firm size, employee benefits and overhead.

16 Based on the number of manager of managers applications submitted since 1995, the staff estimates that 20 additional funds would seek to rely on the proposed rule each year. Approximately 10 of those funds would be funds whose securities have already been publicly offered, and therefore would need to modify their advisory contracts with principal advisers. We estimate that the 10 new funds that would rely on the proposed rule would incur no additional burden hours or costs to include these provisions in the initial advisory contract.

17 In calculating the total annual industry cost of complying with the contract modification (supervision) requirement after the first year, the Commission staff estimated that 40 hours would be incurred by in-house counsel with a wage rate of $312 per hour, 5 hours incurred by fund directors with a wage rate of $2,000 per hour, and 5 hours by clerical staff with an average wage

Proposed rule 15a-5 also would require funds to provide shareholders with an information statement within 90 days after entering into a subadvisory contract or making a material change to a wholly-owned subsidiary's existing subadvisory contract. The information statement must describe the agreement and contain all of the information that shareholders would have received in proxy statement had a shareholder vote been held.[18] During the first 3 years after adoption of the proposed rule, Commission staff estimates that 179 funds[19] would each spend 20 hours[20] annually in preparing and distributing information statements. The total annual burden estimate for complying with the third party disclosure requirement of rule 15a-5 would be 3580 hours. The total estimated annual cost of burden hours is $10,740,000[21] and 358 responses.

To arrive at the total information collection burden, staff has calculated a weighted average of the first year burden and the annual burden thereafter. Using a three-year period, the

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rate of $53 per hour.

18 Proposed rule 15a-5(a)(5).

19 Commission staff estimates that 159 funds (including 125 funds that currently rely on exemptive orders, 14 funds that have filed an application for an exemptive order, and 20 additional funds that would have filed for exemptive relief during the first year after the rule's adoption) would rely on the proposed rule during the first year after its adoption. After the first year, the staff estimates that each year 20 additional funds would rely on the proposed rule.

20 Based on discussions with fund representatives, the Commission estimates that on average each fund would hire 2 new subadvisers per year. Therefore, funds would be required to send to shareholders 2 information statements per year. Based on discussions with fund representatives, the Commission estimates that each fund would spend 10 hours to prepare and mail each information statement.

21 Based on discussions with fund representatives, the Commission estimates that each information statement would cost $30,000 to prepare and distribute. Therefore, each of the 179 funds would spend approximately $60,000 per year to comply with the information statement requirement of the proposed rule.

estimated weighted annual average information collection burden is 3862 hours.[22] The total estimated annual cost of burden hours is $10,868,130[23] and 414 responses.[24]

13. Estimate of Total Annual Cost Burden

The staff does not believe that the proposed rule would entail any annual cost burden for meeting collection of information requirements in addition to the costs of the hourly burden discussed above.

14. Estimate of Cost to the Federal Government

The proposed rule would not entail any costs on the federal government. The proposed rule requires funds to file the information statement that they send to shareholders with the Commission, but funds that rely on the exemptive orders also must file the statement with the Commission. Therefore, the Commission would not incur any new costs from the filing of information statements.

15. Explanation of Changes in Burden

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[22] This estimate is based on the following calculation: (4325 hours (year 1) + 3630 hours (year 2) + 3630 hours (year 3)) ÷ 3 = 3861.6 hours.

[23] The first year burden cost is $11,078,900.50 ($338,900.50 for modification of principal advisory contracts, and $10,740,000 for production and distribution of information statements). The burden cost after the first year is $10,762,745 ($22,745 for modification of principal advisory contracts, and $10,740,000 for production and distribution of information statements). Total cost: ($11,078,900.50) + ($10,762,745) + ($10,762,745) ÷ 3 = $10,868,130.17.

[24] This estimate is based on the following calculation: (507 responses (year 1) + 368 responses (year 2) + 368 responses (year 3)) ÷ 3 = 414.3 responses.

The increase in burden hours is due to an increase in the number of funds that have received a manager of managers exemptive order and also includes additional funds that have applied for such an order.

16. Information Collection Planned for Statistical Purposes

Not applicable.

17. Approval to not Display Expiration Date

Not applicable.

18. Exceptions to Certification Statement

Not applicable.

B. COLLECTION OF INFORMATION EMPLOYING STATISTICAL METHODS

Not applicable.