SUPPORTING STATEMENT FOR
Rule 12d3-1

A. JUSTIFICATION

1. Necessity for the Information Collection

Section 12(d)(3) of the Act generally prohibits a registered investment company ("fund") and companies controlled by the fund from purchasing securities issued by a registered investment adviser, broker, dealer, or underwriter ("securities-related businesses").[1] Rule 12d3-1 permits a fund to invest up to five percent of its assets in securities of an issuer deriving more than fifteen percent of its gross revenues from securities-related businesses, but a fund may not rely on rule 12d3-1 to acquire securities of its own investment adviser or any affiliated person of its own investment adviser.[2]

A fund may, however, rely on an exemption in rule 12d3-1 to acquire securities issued by its subadvisers in circumstances in which the subadviser would have little ability to take advantage of the fund, because it is not in a position to direct the fund's securities purchases. The exemption in rule 12d3-1 is available if: (i) the subadviser is not, and is not an affiliated person of, an investment adviser that provides advice with respect to the portion of the fund that is acquiring the securities; and (ii) the advisory contracts of the subadviser, and any subadviser that is advising the purchasing portion of the fund, prohibit them from consulting with each other concerning securities transactions of the fund, and limit their responsibility in providing advice to providing advice with respect to discrete portions of the fund's portfolio.[3]

1 15. U.S.C. 80a-17(d)(3).

2 *See* 17 CFR 270.12d3-1(b); 17 CFR 270.12d3-1(c)(3).

3 *See* 17 CFR 270.270.12d3-1(c)(3).

2. Purpose of the Information Collection

The rule requires funds to amend their subadvisory contracts before they can rely on rule 12d3-1's exemption to ensure that the subadviser that engages in the transaction does not influence the fund's investment decision to engage in the transaction.

3. Role of Improved Information Technology

To the extent the rule includes recordkeeping requirements, the Electronic Signatures in Global and National Commerce Act[4] and the conforming amendments to recordkeeping rules under the Investment Company Act permit funds to maintain records electronically.

4. Efforts to Identify Duplication

The requirement regarding limitations in the subadviser's contracts is similar to conditions in exemptive rules 10f-3[5], 17a-10[6], and 17c-1[7]. To the extent that a fund relies on more than one of these rules, its subadviser may use the same contract language to satisfy the comparable condition in the other rules.

5. Effect on Small Entities

Rule 12d3-1's exemptive relief is conditioned upon funds including certain provisions in their advisory contracts to ensure that fund interests are the primary consideration for otherwise prohibited transactions; these conditions apply equally to all funds, including small entities.

6. Consequences of Less Frequent Collection

[4] P.L. 106-229, 114 Stat. 464 (June 30, 2000).

[5] 17 CFR 270.10f-3.

[6] 17 CFR 270.17a-10.

[7] 17 CFR 270.17e-1.

Rule 12d3-1 requires that a fund's subadvisory contract be either initially drafted or amended to qualify for the rule's exemption. This is not a recurring requirement; less frequent collection is not possible.

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

Not applicable. The collection is not inconsistent with 5 CFR 1320.5(d)(2).

8. Consultation Outside the Agency

The Commission requested public comment on the collection of information requirements in rule 12d3-1 before it submitted this request for approval to the Office of Management and Budget. The Commission received no comments in response to this request.

More generally, the Commission and the staff at the Division of Investment Management participate in an ongoing dialogue with representatives of the investment company industry through public conferences, meetings, and informal exchanges. These various forums provide the Commission and the staff with a means of ascertaining and acting upon paperwork burdens confronting the industry.

9. Payment or Gift to Respondents

Not applicable.

10. Assurance of Confidentiality

Not applicable.

11. Sensitive Questions

Not applicable.

12. Estimate of Hour Burden

The following estimates of average burden hours are made solely for the purposes of the Paperwork Reduction Act. The estimates are not derived from a comprehensive or even a representative survey or study of the costs of Commission rules.

The Commission staff estimates that 3583 portfolios of approximately 649 fund complexes use the services of one or more subadvisers. Based on discussions with industry representatives, the staff estimates that it requires approximately 6 hours to draft and execute revised subadvisory contracts allowing funds and subadvisers to rely on the exemptions in rule 12d3-1.[8] The staff assumes that all existing funds amended their advisory contracts following amendments to rule 12d3-1 in 2002 that conditioned certain exemptions upon these contractual alterations, and therefore there is no continuing burden for those funds.[9]

Based on an analysis of fund filings, the staff estimates that approximately 600 fund portfolios enter into subadvisory agreements each year.[10] Based on discussions with industry representatives, the staff estimates that it will require approximately 3 attorney hours[11] to draft and execute additional clauses in

8 Rules 12d3-1, 10f-3, 17a-10, and 17e-1 require virtually identical modifications to fund advisory contracts. The Commission staff assumes that funds would rely equally on the exemptions in these rules, and therefore the burden hours associated with the required contract modifications should be apportioned equally among the four rules.

9 We assume that funds formed after 2002 that intended to rely on rule 12d3-1would have included the contract provision in their initial subadvisory contracts.

10 The use of subadvisers has grown rapidly over the last several years, with approximately 600 portfolios that use subadvisers registering between December 2005 and December 2006. Based on information in Commission filings, we estimate that 31 percent of funds are advised by subadvisers.

11 The Commission staff's estimates concerning the wage rates for attorney time are based on salary information for the securities industry compiled by the Securities Industry Association.

new subadvisory contracts in order for funds and subadvisers to be able to rely on the exemptions in rule 12d3-1. Because these additional clauses are identical to the clauses that a fund would need to insert in their subadvisory contracts to rely on rules 10f-3, 17a-10, and 17e-1, and because we believe that funds that use one such rule generally use all of these rules, we apportion this 3 hour time burden equally to all four rules. Therefore, we estimate that the burden allocated to rule 12d3-1 for this contract change would be 0.75 hours.[12] Assuming that all 600 funds that enter into new subadvisory contracts each year make the modification to their contract required by the rule, we estimate that the rule's contract modification requirement will result in 450 burden hours annually, with an associated cost of approximately $131,400.[13]

13. Estimate of Total Annual Cost Burden

We estimated that there is no cost burden of rule 12d3-1, other than the respondent recordkeeping burden identified in Item 12 of this Supporting Statement. Compliance with the rule is part of customary and usual investment company business practice to ensure compliance with applicable laws and regulations.

14. Estimate of Cost to the Federal Government

There are no costs to the Federal Government associated with rule 12d3-1.

15. Explanation of Changes in Burden

The $292 per hour figure for an attorney is from the SIA *Report on Management & Professional Earnings in the Securities Industry 2006*, modified to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

12 This estimate is based on the following calculation (3 hours ÷ 4 rules = .75 hours).

13 These estimates are based on the following calculations: (0.75 hours × 600 portfolios = 450 burden hours); ($292 per hour × 450 hours = $131,400 total cost).

Rule 12d3-1 has a current annual burden of 117 hours. The hour burden associated with rule 12d3-1 has increased to 450 hours since our last burden analysis due to an increase in the number of funds using subadvisers and revised estimates for the hourly burden of complying with the rule. The information we received during our discussions with fund representatives and updated salary information has led us to request an increase in the estimated annual burden and annual cost. We now estimate that funds that rely on rule 12d3-1 incur an annual burden of 450 hours instead of the previously estimated 117 burden hours, for a total increase of 333 burden hours.

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. COLLECTIONS OF INFORMATION EMPLOYING STATISTICAL METHODS

Not applicable.