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January 8, 2020

Ms. Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: **Use of Central Funds in Fund of Funds Arrangements (File No. S7-27-18)**

Dear Ms. Countryman:

We write to supplement the comment letter we submitted to the Securities and Exchange Commission (the "Commission") on May 2, 2019 (the "Initial Comment Letter") on the Commission's above-referenced proposal regarding fund of funds arrangements (the "Proposed Rule").[1] We appreciate the opportunity to provide additional comment on the Proposed Rule, expanding on our comments in the Initial Comment Letter regarding the use of central funds in funds-of-funds arrangements. As noted in the Initial Comment Letter, the Capital Group Companies is one of the oldest asset managers in the United States. Through our investment management subsidiaries, we actively manage assets in various collective investment vehicles and institutional client separate accounts globally. The majority of these assets consist of the American Funds family of mutual funds, which are U.S. regulated investment companies distributed through financial intermediaries and held by individuals and institutions across different types of accounts. As part of the American Funds, we manage approximately $200 billion in proprietary fund-of-funds assets in reliance on Section 12(d)(1)(G) of the Investment Company Act of 1940 (the "Act").

We believe certain modifications to the Proposed Rule are necessary in order to minimize disruption to the value investment advisers provide to investors through fund of funds structures and to level the competitive playing field by allowing all investment advisers to use central funds as third-tier funds in fund of funds arrangements, subject to certain conditions to alleviate the

[1] Fund of Funds Arrangements, Release No. 33-10590 and IC-33046 (Dec. 19, 2018), 84 Fed. Reg. 1286 (Feb. 1, 2019).

Commission's concerns with three-tier structures. As drafted, the Proposed Rule would prohibit most three-tier funds-of-funds arrangements, subject to limited exceptions. The Proposed Rule further contemplates the termination of prior fund-of-funds exemptive and no-action relief, which would likely require the various funds-of-funds operating in reliance on such no-action letters and exemptive orders to be restructured.

We believe that any final rule adopted by the Commission should allow second-tier funds in fund of funds arrangements relying on Section 12(d)(1)(G) to invest in a third-tier "central fund" in order to centralize the portfolio management of investments in various asset classes (e.g., investment grade corporate bonds, mortgage-backed securities or high yield securities). We also believe, consistent with the views of industry associations and other participants, that current exemptive and no-action relief allowing this type of three-tiered structure should either be reflected in any final rule or not be rescinded.[2] We currently do not have exemptive relief permitting the use of central funds in our fund of funds arrangements but would like to obtain such relief if such relief is not reflected in any final rule. We would further hope that any final rule would not present a bar to obtaining such exemptive relief.

As the Commission acknowledged in the Proposed Rule, three-tier structures involving central funds "provide efficient and cost-effective exposure to certain market segments."[3] By aggregating assets in an asset class and centralizing the management of such investments, these arrangements improve portfolio management and operational efficiency (through reduced trading and settling costs) and, at the same time, provide exposure to a more broadly diversified set of securities in an asset class. These arrangements have been beneficial to investors investing with fund families that rely on exemptive orders or no-action letters combined with relief provided under Section 12(d)(1)(G) of the Act to implement such arrangements. Subject to certain restrictions described

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[2] *See*, e.g., Investment Company Institute Comment Letter on April 30, 2019 in response to the Proposed Rule, available at https://www.sec.gov/comments/s7-27-18/s72718-5433908-184637.pdf; Pacific Investment Management Company LLC (PIMCO) Comment Letter on May 1, 2019 in response to the Proposed Rule, available at https://www.sec.gov/comments/s7-27-18/s72718-5439453-184808.pdf; Fidelity Investments Comment Letter on May 2, 2019 in response to the Proposed Rule (the "Fidelity Investments Comment Letter"), available at https://www.sec.gov/comments/s7-27-18/s72718-5444921-184870.pdf; Asset Management Group of the Securities Industry and Financial Markets Association (SIFMA) Comment Letter on May 2, 2019 in response to the Proposed Rule, available at https://www.sec.gov/comments/s7-27-18/s72718-5444905-184855.pdf; and Federated Investors, Inc. Comment Letter on June 7, 2019 in response to the Proposed Rule, available at https://www.sec.gov/comments/s7-27-18/s72718-5646600-185667.pdf.
[3] Proposed Rule at 83.

further below, we believe these three-tier structures involving central funds offer benefits to investors without the risks with which the Commission is concerned.

1. Relevant Law and Existing Relief for Fund-of-Funds Arrangements with Central Funds

a. Relevant Law

Under Section 12(d)(1)(A) of the Act, a registered investment company is prohibited from acquiring shares of an investment company if, immediately after the acquisition, the securities represent: (i) more than 3% of the total outstanding voting stock of the acquired company (the "3% Limit"); (ii) more than 5% of the total assets of the acquiring company (the "5% Limit"); or (iii) together with the securities of any other investment companies, more than 10% of the total assets of the acquiring company (the "10% Limit" and, together with the 3% Limit and the 5% Limit, the "12(d)(1)(A) Limits").

Section 12(d)(1)(G) of the Act, in relevant part, provides a conditional exemption from the 12(d)(1)(A) Limits for certain fund-of-funds arrangements within the same group of investment companies. One of the conditions in Section 12(d)(1)(G) requires an underlying fund to have a policy that prohibits it from investing in shares of other investment companies in reliance on Section 12(d)(1)(F) or (G) of the Act. A second-tier fund thus requires exemptive relief from the above restriction in order to be able to invest in a central fund in excess of any of the 12(d)(1)(A) Limits.

b. T. Rowe Price Exemptive Order (2003)

On April 8, 2003, the Commission issued an exemptive order allowing a T. Rowe Price "Upper-Tier Fund" in which the T. Rowe Price Spectrum Fund, Inc. (the "Spectrum Fund") invests to purchase the shares of an underlying fund (the "Underlying Fund") in excess of the 3% Limit (the "T. Rowe Price Exemptive Order").[4] The Underlying Fund in question was the T. Rowe Price Institutional High Yield Fund, which invested in high yield bonds with the intent to "provide a more efficient and cost-effective means of investing assets" of the Upper-Tier Fund as well as others allocated to high-yield securities. Note, however, that the T. Rowe Price Exemptive Order applies to other T. Rowe

[4] *In re T. Rowe Price Balanced Fund, Inc.*, Release No. 25996 (2003) (order).

Price Underlying Funds that comply with the conditions of the order, regardless of the asset class of their investments.

The T. Rowe Price Exemptive Order explicitly allows for a three-tier fund-of-funds structure in which the second-tier fund may invest in a third-tier fund in excess of the 3% Limit, subject to the conditions set forth in the relief. These conditions require, among other things, that (i) the funds continue to comply with the 5% Limit and the 10% Limit and, to the extent not inconsistent with the relief granted in the T. Rowe Price Exemptive Order, with Section 12(d)(1)(G), (ii) the board of directors/trustees of the Upper-Tier Fund (including a majority of directors/trustees who are not "interested persons" as defined in Section 2(a)(19) of the Act) find, prior to approving any advisory contract, that any advisory fees charged under any advisory contract are not duplicative of fees charged pursuant to the advisory contract of the Underlying Fund and (iii) any sales charges or service fees charged with respect to securities of the Spectrum Fund, when aggregated with (x) those paid by the Spectrum Fund with respect to securities of the Underlying Fund and (y) those paid by the Underlying Fund with respect to securities acquired in compliance with the 5% Limit and the 10% Limit, not exceed the limits set forth in Rule 2830 of the National Association of Securities Dealers, Inc. (NASD). We believe this is a good example of how three-tier fund-of-funds arrangements involving central funds have been implemented subject to appropriate restrictions, and one that the Commission might reference as a guidepost as it considers potential revisions to the Proposed Rule.

c. Additional Exemptive Orders

Over the years, the Commission has issued numerous exemptive orders to funds-of-funds from the requirements of Section 12(d)(1)(A) and/or Section 12(d)(1)(B) as they pertain to affiliated funds. While these exemptive orders do not explicitly discuss three-tier fund-of-funds structures, they have been relied upon – in combination with Section 12(d)(1)(G) relief – to enable fund families to effectuate three-tier fund-of-funds arrangements.[5]

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[5] *See* the Proposed Rule at 96 (the Commission making the same observation, noting that "[a]lthough section 12(d)(1)(G) requires an acquired fund to have a policy that prohibits it from acquiring any securities of a registered open-end fund or UIT in reliance on section 12(d)(1)(G) or (F), it does not require the acquired fund to have a policy that prohibits it from acquiring the securities of a fund beyond the limits in section 12(d)(1)(A) in reliance on an exemptive order issued by the Commission"); *see also* Fidelity Investments Comment Letter at 21 (noting, with respect to its three-tier fund of funds structure, that "[t]he funds investing in another fund at each tier of the structure do so pursuant to an SEC exemptive order granted to Fidelity or

d. Franklin Templeton Investments No-Action Letter (2015)

On April 3, 2015, the Staff issued a No-Action Letter to Franklin Templeton Investments ("FTI"), permitting a three-tier arrangement whereby a top-tier fund invests in a second-tier fund that, in turn, invests in a third-tier central fund holding certain floating rate instruments (a "FTI Central Fund") in excess of the 3% Limit.[6] The FTI Central Fund was intended to help realize certain efficiencies by aggregating and centralizing the management of investments in a particular asset class. FTI's arrangement was subject to similar conditions (if not the same) as those contained in the T. Rowe Price Exemptive Order, including that the funds comply with the 5% Limit and the 10% Limit and otherwise with Section 12(d)(1)(G) as described in Part 1(b) above, that management fees otherwise payable by the second-tier fund to the investment adviser be off-set against those paid by the FTI Central Fund to the investment adviser, that the FTI Central Fund not acquire securities of any investment company relying on Section 3(c)(1) or 3(c)(7) of the Act in excess of the 12(d)(1)(A) Limits, and that shares of the FTI Central Fund not be subject to a sales load, redemption fee or a distribution fee under a plan adopted in accordance with Rule 12b-1 under the Act. However, the FTI no-action letter also included a condition that shares of the FTI Central Fund would be sold solely to the top-tier fund and the second-tier fund (the "Funds Only Condition"). We believe that the Funds Only Condition is too restrictive and suggest an alternative below to address the Commission's concerns in this area. While the central fund described in the FTI No-Action Letter was one invested in floating rate securities, the FTI No-Action Letter noted that FTI's request for relief extended to "other situations where FTI Managers manage certain categories of assets or securities in the portfolios of multiple Funds and where similar efficiencies could be realized by aggregating those assets or securities in a Central Fund."[7]

2. Public Policy Considerations

In our Initial Comment Letter, we noted, as we do here, the merits of a third-tier "central fund" and the opportunity for the Commission to expand such concept beyond money funds to other asset classes. At the same time, recognizing the Commission's concerns regarding issues of complexity

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an SEC rule"); *see also* fn.9 of *T. Rowe Price Balanced Fund, Inc., Et Al.* Application for Exemptive Order (File No. 812-12891), as amended (Mar. 13, 2003) (citing to precedent).

[6] *Franklin Templeton Investments*, Staff No-Action Letter (pub. avail. Apr. 3, 2015) ("FTI No-Action Letter").

[7] *Id. at fn. 3.*

and layering of fees posed by three-tier fund of funds arrangements, we proffer two potential conditions designed to alleviate these concerns for the Commission's consideration: (i) first, that the central fund be available only to funds within its same group of funds and other collective investment vehicles and accounts managed by the same investment advisor or its affiliated investment advisors, and (ii) second, that the central fund not impose any type of fees (other than for legitimate fund expenses such as custodial, audit, legal and board fees) or commissions. We believe that these conditions, coupled with certain other limitations set forth in the T. Rowe Price Exemptive Order, including continued compliance with the 5% Limit and the 10% Limit, would mitigate the Commission's concerns with complexity and the layering of fees in multi-tier structures. Further, to address potential structural complexity, the Commission could prohibit the central fund in question from acquiring securities of any investment company or company relying on Section 3(c)(1) or 3(c)(7) of the Act in excess of the 12(d)(1)(A) Limits.

With these guardrails, we believe investment managers would be able to implement funds-of-funds arrangements involving central funds for the benefit of their investors while mitigating any harm resulting from duplicative fees or structural complexity.

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We thank the Commission for its consideration of our above comments as well as those in our Initial Comment Letter, which we believe align with the goals of the Proposed Rule and are intended to make fund of funds arrangements as valuable as possible for investors. If you have any questions or would like to discuss the contents of this letter, please feel free to contact me at [redacted].

Sincerely,

Michael J. Triessl
Senior Vice President and Senior Counsel
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