Your letter of March 13, 1997 requests our assurance that we would not recommend that the Commission take any enforcement action against AmSouth Mutual Funds ("Trust") under the Investment Company Act of 1940 if, for the period from March 20, 1997 to July 31, 1997, the Trust's securities and similar investments are verified twice by its independent public accountants rather than three times, as required by Rule 17f-2(f). 

The Trust has been in operation since 1988. In your letter, you state that the Trust would become subject to the requirements of Rule 17f-2(f) on March 20, 1997, when AmSouth Bank of Alabama, the Trust's investment adviser, would begin to serve as the Trust's custodian. Because the Trust's fiscal year ends on July 31, there will be a "stub" fiscal period of four and one-half months during which the Trust will be subject to the verification requirements of the rule.

You believe that requiring three verifications within such a short period of time does not further the policies underlying

1/ Under Rule 17f-2, which applies to registered investment companies that maintain self-custody of their assets, an investment company must have its securities and similar investments verified by actual examination by an independent public accountant at least three times during each fiscal year. At least two of these examinations must be at times chosen by the accountants without prior notice to the fund.

2/ Subsequent to submitting your letter, you advised us that AmSouth Bank of Alabama actually began serving as custodian for one of the funds in the Trust on March 17, 1997, and for all other funds in the Trust on April 17, 1997. Telephone conversation between Daniel E. Burton and Francoise M. Haan on June 30, 1997. These revised facts do not affect our analysis or conclusion set forth in this letter.

3/ The staff has taken the position that the self-custody provisions of Rule 17f-2 apply when a fund's investment adviser also serves as the fund's custodian. See The Mutual Fund Group (pub. avail. Dec. 12, 1989); Pegasus Income & Capital Fund, Inc. ("Pegasus") (pub. avail. Dec. 31, 1977).
Rule 17f-2 4/ and imposes an unnecessary cost on the Trust with limited additional benefits. You propose to have one "surprise" verification during the Trust’s stub fiscal period, in addition to the Trust's regular fiscal year-end verification. 5/ You maintain that, in the case of the Trust, the policy of subjecting a fund’s securities to adequate independent scrutiny would not be compromised by reducing the number of required annual verifications from three to two. You believe that two verifications -- one surprise verification and one at fiscal year-end -- over a four and one-half month period would be adequate to protect the Trust’s investors.

The staff previously has granted no-action relief under Rule 17f-2(f) to funds with a stub fiscal period of less than six months during the fund’s first year of operations. 6/ Although the fiscal year ending July 31, 1997 is not the Trust’s first year of operations, it will be the first fiscal year during which the Trust will be subject to the self-custody rule. Thus, granting the requested relief is consistent with the staff’s prior letters.

We would not recommend enforcement action to the Commission under Section 17(f) of the Investment Company Act or Rule 17f-2(f) thereunder if, during the Trust’s stub fiscal period ending July 31, 1997, the Trust’s securities and similar

4/ It is a principal policy of the Investment Company Act, as expressed generally in Section 1(b)(5) and specifically in Section 17(f), to ensure that securities owned by investment companies are maintained in such a manner that they will be subject to adequate independent scrutiny. Pegasus, supra note 3.

5/ You represent that, in all subsequent fiscal years in which the Trust’s adviser also acts as the Trust’s custodian, three verifications will be made, in accordance with Rule 17f-2(f).

6/ See Morgan Stanley Emerging Markets Fund, Inc. ("Morgan Stanley") (pub. avail. Dec. 30, 1991) (two verifications, one without prior notice on a date chosen by the fund’s accountant and the other as of the fund’s fiscal year-end, during a stub period of slightly more than two months); The Sessions Group (pub. avail. Mar. 26, 1990) (two verifications, timed as in Morgan Stanley, during a fiscal period of five months); The Seven Seas Series Fund ("Seven Seas") (pub. avail. May 26, 1988) (two verifications, timed as in Morgan Stanley, during a stub period of approximately four months). In Seven Seas, the staff noted that, as a general matter, it will not grant no-action relief under Rule 17f-2(f) in situations involving either a change in a fund’s fiscal year-end during any year of operations, or a stub fiscal period of six months or more for a fund’s first fiscal year of operations.
investments are verified two times by its independent public accountants, rather than the three times required by Rule 17f-2(f), provided that the timing of one verification is chosen by the accountants without prior notice to the Trust and the other is the Trust’s regular fiscal year-end verification. 21

This response expresses the Division’s position on enforcement only, and does not purport to express any legal conclusions on the questions presented. Because this position is based on the facts and representations made in your letter, you should note that any different facts or circumstances might require a different conclusion.

Daniel E. Burton
Attorney

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21 We previously informed you of this position in a telephone conversation between Daniel E. Burton and Francoise M. Haan on March 20, 1997.
March 13, 1997

VIA MESSENGER

Office of the Chief Counsel
Division of Investment Management
Securities and Exchange Commission
450 Fifth Street, N.W.
Judiciary Plaza
Washington, D.C. 20549

Re: AMSOUTH MUTUAL FUNDS (the "Trust")
Securities Act of 1933 Registration No.
Investment Company Act of 1940 File No. 811-5551

Dear Sir or Madam:

We hereby request that you advise us that the Division of Investment Management (the "Division") will not recommend that the Securities and Exchange Commission (the "Commission") take action against the Trust if, for the period from March 20, 1997 to July 31, 1997, the Trust's securities and similar investments are verified twice by its independent public accountants rather than the three times required under Rule 17f-2(f) of the Investment Company Act of 1940, as amended (the "1940 Act"), for full fiscal years. The two verifications would include the Trust's regular year-end verification and one chosen by the Trust's independent public accountants without prior notice.
BACKGROUND

AmSouth Mutual Funds is a Massachusetts Business Trust registered as an open-end management investment company. Beginning on March 20, 1997, AmSouth Bank of Alabama, which serves as the Trust's Investment Advisor, will begin serving as Custodian to the Trust as well.

Rule 17f-2(f) of the 1940 Act applies to registered investment companies which maintain in their own custody their securities and similar investments, and generally provides that during any fiscal year an independent public accountant must verify such company's securities and similar investments at least three times a year, at least two of which shall be at the selection of the accountant without prior notice to the company. The Commission's staff has interpreted Rule 17f-2(f) as also applying to a registered investment company whose investment advisor also serves as its custodian. Pegasus Income & Capital Fund, Inc. (available December 31, 1977); Carnegie-Cappiello Growth Trust (available August 8, 1985).

The Rule is clear as to its application to full fiscal years. Whether the Rule requires three audits during the Trust's first partial fiscal period with self-custody, however, is unclear.

DISCUSSION AND ANALYSIS

Although the Trust has been in operation since 1988, it will only begin self-custody, by virtue of AmSouth Bank of Alabama assuming the function of custodian, on March 20, 1997. Because the Trust's fiscal year ends on July 31, 1997, this will result in a partial fiscal year of only four and one half months with AmSouth Bank of Alabama as custodian. If the requirements of Rule 17f-2(f) are interpreted as being applicable to a partial fiscal year, then the Trust's securities and similar investments must be verified three times during these four and one half months of operation.

The Commission's staff has previously stated that it would not recommend enforcement action against a registered investment company under circumstances very similar to those of the Trust. The Riverfront Funds, Inc. (available November 8, 1995), Morgan Stanley Emerging Markets Fund, Inc. (available December 30, 1991), The Sessions Group (available March 26, 1990), and The Seven Seas Series Fund (available May 26, 1988). Each of the registered investment companies which received these no-action letters had a short initial fiscal year period; three months in the case of the Riverfront Funds, two months for Morgan Stanley Emerging Markets Fund, Inc., five months for the Sessions Group and four months for the Seven Seas Series Fund. In the case of the Riverfront Funds, the Commission's staff granted no-action relief where the Riverfront Funds, like the Trust, had had previous operations but had not previously been subject to the self-custody provisions of Rule 17f-2.
While the Commission’s staff in The Seven Seas Series Fund letter did not give any specific advice with respect to initial fiscal periods in the Trust’s particular circumstances, in footnote no.2 the staff did provide that "as a general matter, the staff will not grant no-action relief in situations involving either a change in a fund’s fiscal year-end during any year of operations or a stub fiscal year of six months or more for a fund’s first fiscal year of operation." Therefore, while the staff's position is clear that it generally will not grant such relief for stub fiscal periods of six months or more, it is not clear whether the staff would grant such relief in a situation such as the Trust's.

We believe, however, that requiring three verifications within such a short period of time as four and one half months does not further the policies underlying Rule 17f-2(f) and, thus, imposes an unnecessary cost on Trust shareholders with limited additional benefits.

The staff has stated that it is a principal policy of the 1940 Act, as expressed generally in Section 1(b)(5) and specifically in Section 17(f), to ensure that securities owned by investment companies are subject to adequate independent scrutiny. Pegasus Income & Capital Fund, supra. This policy is accomplished by requiring verification of the holdings of investment companies by independent accountants and, in the case of self-custody, an additional two surprise inspections by those accountants to reduce the likelihood of embezzlement and larceny.

In the case of the Trust, the policy of independent scrutiny would not be compromised by reducing the number of required verifications from three to two. Two verifications, one a surprise and one at the end of the Trust’s first fiscal period, are adequate in a four and one half month period to protect the Trust's investors. A third verification increases the cost to shareholders with only nominal, if any, additional benefits.

**CONCLUSION**

Based on the discussion and analysis set forth above, we respectfully request that the Division not recommend that the Commission take action against the Trust if, for the Trust’s first fiscal period with self-custody beginning on March 20, 1997 and ending July 31, 1997, the Trust’s securities and similar investments are verified two times by its accountants, one being a surprise verification, and the other being the Trust’s regular year-end verification. In all subsequent fiscal years of the Trust, three verifications will be made in accordance with the requirements of Rule 17f-2(f).
In order to avoid the costs associated with a third verification, we would appreciate your prompt attention to this matter. If we may be of any assistance in expediting your review or may answer any questions you may have, please do not hesitate to contact me at 202-626-3913.

Sincerely,

Francoise M. Haan

cc: John F. Calvano
    Alan G. Priest

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