



VIA HAND DELIVERY

December 28, 2006



Nancy M. Morris, Esq.  
Secretary  
U.S. Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549

Re: Petition for Rulemaking - Funds of Funds Disclosure and Unregistered Investment Vehicles

Dear Ms. Morris:

Fidelity Management & Research Company ("Fidelity")<sup>1</sup> writes to you with respect to the disclosure requirements adopted by the U.S. Securities and Exchange Commission ("Commission") relating to investments by registered investment companies in certain underlying investment vehicles.<sup>2</sup> The form amendments adopted in the Fund of Funds Release aim to provide investment company shareholders with greater transparency and disclosure regarding fund expenses associated with fund investments in other investment funds ("lower-tier funds"). Investment by registered (or unregistered) investment companies in lower-tier funds is regulated by Section 12(d)(1) of the Investment Company Act of 1940, as amended (the "1940 Act"), which restricts the investment activities of "investment companies".

We are generally supportive of the new disclosure requirements but believe that they are overly broad with respect to certain types of entities that rely on Section 3(c)(1) or Section 3(c)(7) of the 1940 Act to avoid registration thereunder.<sup>3</sup> As discussed more fully below, we believe that

<sup>1</sup> Fidelity Investments is one of the world's largest providers of financial services, with custodied assets of more than \$2.8 trillion, including managed assets of over \$1.3 trillion as of October 31, 2006. Fidelity offers investment management, retirement planning, brokerage, and human resources and benefits outsourcing services to more than 22 million individuals and institutions as well as through 5,500 financial intermediary firms.

<sup>2</sup> See *Fund of Funds Investments*, Investment Company Act Rel. No. 27399 (June 20, 2006) (the "Fund of Funds Release").

<sup>3</sup> Sections 3(c)(1) and 3(c)(7) of the 1940 Act exclude certain entities from the definition of "investment company" under the 1940 Act. Section 3(c)(1) excepts from the definition of investment company, an issuer the securities (other than short-term paper) of which are

the cost and effort that will be required to obtain the relevant fee information from these types of vehicles is entirely disproportionate to the benefit, if any, that shareholders will obtain from receiving this information. Moreover, the new disclosure requirements, as they apply to vehicles that rely on Section 3(c)(1) or Section 3(c)(7), appear to go beyond the Commission's traditional areas of concern in the fund of funds arena. For example, regulation of funds of funds investments traditionally has been justified because of the possibility that certain services, fees and expenses might be duplicated by both the upper- and lower-tier funds (among other reasons). However, under the new disclosure requirements, registrants may be required to reflect in their operating expenses the expenses and fees of issuers that are operationally distinct from investment companies and that do not typically raise concerns regarding duplication of services, fees and expenses.

While we understand the Commission's interest in expanding its traditional fund of funds focus to address registered investment company investments in certain types of vehicles that do rely on Section 3(c)(1) or Section 3(c)(7), such as hedge funds, we do not believe that all vehicles relying on these sections raise similar concerns and should be categorized together. Accordingly, we are hereby petitioning the Commission to amend the disclosure requirements under the 1940 Act, pursuant to Section 6(c) thereof, to limit the application of the new disclosure requirements to registered investment company investments in "investment companies" and "private funds", as defined in former Investment Advisers Act Rule 203(b)(3)-1(d) ("Private Funds").<sup>4</sup>

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beneficially owned by not more than 100 persons and that is not making or proposing to make a public offering of its securities. An issuer that is organized in a country other than the United States is not subject to the 100-investor limitation of Section 3(c)(1) with respect to its beneficial owners who are non-U.S. persons. Section 3(c)(7) excepts from the definition of investment company, an issuer the outstanding securities of which are owned exclusively by persons who, at the time of acquisition of such securities, are "qualified purchasers" (as defined in Section 2(a)(51)) and that is not making or proposing to make a public offering of its securities. An issuer that is organized in a country other than the United States is not subject to the qualified purchaser limitation of Section 3(c)(7) with respect to its owners who are non-U.S. persons. Broadly, Section 3(c)(1) and Section 3(c)(7) issuers are excluded from most 1940 Act regulation due to lessened regulatory concern with respect to their operation as essentially private companies selling shares to investors that the Commission has recognized do not need the full extent of the investor protections afforded by the Securities Act of 1933 and the 1940 Act.

<sup>4</sup> Rule 203(b)(3)-1(d) defined a Private Fund as (1) a company:

- (i) That would be an investment company under section 3(a) of the Investment Company Act of 1940 (15 U.S.C. 80a-3(a)) but for the exception provided from that definition by either section 3(c)(1) or section 3(c)(7) of such Act (15 U.S.C. 80a-3(c)(1) or (7));

## I. The New Disclosure Requirements

### A. Summary of Disclosure Requirements

The new disclosure requirements as set forth in the Fund of Funds Release and investment company registration forms generally provide that an “acquiring fund” (i.e., a registered investment company investing in another fund) include in the fee table in its prospectus a line item that discloses the acquiring fund’s pro rata portion of the cumulative net operating expenses and transaction fees charged by lower-tier funds in which the acquiring fund invests. The costs are included in the acquiring fund’s total annual operating expenses, and also reflected in the acquiring fund’s expense example.

The purpose of these new requirements is to help investors understand the full costs of investing in a fund of funds, both to assist them in comparing the costs of investing in alternative funds of funds and in comparing the costs of an investment in a fund of funds with the cost of investing in a more traditional fund. To this end, the new disclosure requirements also require that a registered fund disclose the costs of investing in not only registered investment companies,

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(ii) That permits its owners to redeem any portion of their ownership interests within two years of the purchase of such interests; and

(iii) Interests in which are or have been offered based on the investment advisory skills, ability or expertise of the investment adviser.

(2) Notwithstanding paragraph (d)(1) of this section, a company is not a private fund if it permits its owners to redeem their ownership interests within two years of the purchase of such interests only in the case of:

(i) Events you find after reasonable inquiry to be extraordinary; and

(ii) Interests acquired through reinvestment of distributed capital gains or income.

(3) Notwithstanding paragraph (d)(1) of this section, a company is not a private fund if it has its principal office and place of business outside the United States, makes a public offering of its securities in a country other than the United States, and is regulated as a public investment company under the laws of the country other than the United States.

*See also Registration Under the Advisers Act of Certain Hedge Fund Advisers, Investment Advisers Act Rel. No. 2333 (Dec. 2, 2004) (the “Hedge Fund Adviser Release”).*

but also “any unregistered fund that would be an investment company under [S]ection 3(a) of the [1940] Act but for the exceptions provided in [S]ections 3(c)(1) and 3(c)(7) of the [1940] Act”.<sup>5</sup>

*B. Summary of Reasons for Requested Changes to the Disclosure Requirements*

As explained more fully below, Congress and the Commission generally have not extended the Commission’s regulation of funds to funds to investments by an investment company in Section 3(c)(1) and Section 3(c)(7) issuers, although they have over time limited the investment by such issuers in investment companies. Accordingly, the disclosure requirements are inconsistent with the regulatory focus on investments by Section 3(c)(1) and Section 3(c)(7) issuers in investment companies.

The scope of the new disclosure requirements covers the following types of entities:

- Investment companies (registered or unregistered).<sup>6</sup>
- Hedge funds, which may rely on the Section 3(c)(1) and Section 3(c)(7) exclusions.<sup>7</sup> For purposes of this petition, we consider the term “Private Funds” to include “hedge funds”.
- Entities, such as private equity funds,<sup>8</sup> that participate in the management of operating companies and that rely on the Section 3(c)(1) and Section

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<sup>5</sup> Fund of Funds Release at fn. 80 and accompanying text, specifically citing to the example of a cash sweep arrangement in an unregistered money market fund.

<sup>6</sup> Note that since both Section 3(c)(1) and Section 3(c)(7) exclude issuers that meet the conditions of either section from the 1940 Act definition of “investment company,” such entities are not considered to be unregistered investment companies. Rather, an unregistered investment company is an investment company that is not subject to the regulatory jurisdiction of the Commission (e.g., an offshore issuer that is not offering its securities in the U.S.).

<sup>7</sup> While there is no precise definition of the term, hedge funds are generally understood to be investment pools sponsored by investment advisers with redemption features that offer investors a right to withdraw their assets from management, based on their individual liquidity needs and other preferences. These characteristics formed the basis for the Commission’s rulemaking with respect to Private Funds. Hedge Fund Adviser Release, at fn 223-245 and accompanying text.

<sup>8</sup> In spite of the similarity in their names, a private equity fund is conceptually distinct from a Private Fund because of the active involvement in portfolio company management in the case of the former. See e.g. Staff Report to the United States Securities and Exchange Commission, “Implications of the Growth of Hedge Funds” (September 2003) at 7-8 (*avail. at* <http://www.sec.gov/news/studies/hedgcfunds0903.pdf>) (discussion of private equity and venture capital funds).

- 3(c)(7) exclusions. In this petition, we refer to such entities as “operating company conduits”.
- Structured finance vehicles that rely on the Section 3(c)(1) and Section 3(c)(7) exclusions.<sup>9</sup>

Certain of these issuers—specifically operating company conduits and structured finance vehicles—are operationally distinct from investment companies and Private Funds, and, as discussed below, do not generally implicate the regulatory concerns underlying regulation of funds of funds arrangements. Accordingly, they should not be subject to funds of funds regulation.

In light of the above, we propose that the application of the new disclosure requirements be limited only to registered investment company investments in investment companies (registered or unregistered) and Private Funds.<sup>10</sup> We believe that entities, investment in which has not traditionally been regulated by Section 12(d)(1), generally should be excluded from the new disclosure requirements. We recognize that the proliferation of hedge funds, as well as the functional similarity of many hedge funds to investment companies, represent exceptional circumstances that may warrant a departure from the traditional scope of regulation under Section 12(d)(1). However, operating company conduits and structured finance vehicles, for which disclosure would be less comparable, less reliable and/or less useful, would accordingly not be subject to the new disclosure requirements.<sup>11</sup>

Our arguments in support of our proposal are set forth below in Section II.

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<sup>9</sup> Structured finance vehicles include, without limitation, issuers of collateralized debt obligations, collateralized mortgage obligations, residential mortgage-backed securities, commercial mortgage-backed securities, other types of asset-backed securities and commercial paper notes.

<sup>10</sup> The proposed definition of Private Fund will also capture entities that closely resemble registered investment companies, such as unregistered money market funds.

<sup>11</sup> We agree with the approach to rulemaking exemplified by the Hedge Fund Advisers Release and believe that a bright-line rule defining the entities that should be subject to the regulation in question is preferable to a piecemeal approach pursuant to which operating company conduits and structured finance vehicles would be defined and excepted from disclosure requirements.

## II. Discussion

The new disclosure requirements apply to investments in all Section 3(c)(1) and Section 3(c)(7) issuers. As an initial matter, we believe that an overly broad application of the new disclosure requirements is not constructive for investors and generally should be discouraged. Broad application of the requirements places additional burdens on registrants, which must try to derive expense information relating to lower-tier vehicles. The Commission acknowledged the potential difficulty of this task in the Fund of Funds Release and the disclosure requirements by permitting registrants to derive this information from various sources, including estimates based on written fee arrangements or information derived from shareholder communications. However, reliable expense information will not necessarily be available with respect to all unregistered lower-tier vehicles.<sup>12</sup> The increased burden and uncertainty placed on registered investment companies, and the underlying issuers, of complying with a broad application of the new disclosure requirements conceivably could impede capital formation and reduce the attractiveness of these issuers to institutional investors such as registered investment companies. Alternatively, the added costs of obtaining fee information could increase fund expenses.

### A. *Section 3(c)(1) and 3(c)(7) Issuers Have Not Traditionally Raised Fund of Funds Concerns*

The Commission traditionally has not applied fund of funds regulation to investment company investments in Section 3(c)(1) and Section 3(c)(7) issuers. As originally enacted, Section 12(d)(1) of the 1940 Act limited the interest in any "investment company" (whether registered or unregistered) that a registered investment company could acquire. Because Section 3(c)(1) issuers are not investment companies, the Section 12(d)(1) limits on investment in investment companies did not extend to ownership of 3(c)(1) issuers. Section 3(c)(7) was yet to be enacted. Separately from the Section 12(d)(1) requirements, Section 3(c)(1) effectively limited corporate investors (including investment companies) in Section 3(c)(1) issuers to acquiring less than 10% of a Section 3(c)(1) issuer's outstanding voting securities by attributing ownership of a 10% owner's interest to the holders of the 10% owner's outstanding shares. This

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<sup>12</sup> For example, although reports relating to the pooled assets in a structured finance vehicle and separate reports relating to periodic payments to investors and service providers to structured finance vehicles are routinely provided on a monthly or quarterly basis to trustees, managers, servicers, administrators, rating agencies and monoline insurers, if any, who may wrap the senior-most classes of rated notes, such reports typically do not include information relating to all of the expenses paid by such vehicles since such expenses may be paid intraperiod subject to capped amounts or certain reserves provided for in the transaction documents. In addition, such reports are typically available to investors only upon request and must be requested by the registered owner of the securities, which is frequently the Depository Trust Company. Thus, even if expense information is available in the reports, an investment company which is the beneficial owner of the securities would have to request such reports through the Depository Trust Company.

provision of Section 3(c)(1) was designed to safeguard the non-public character of Section 3(c)(1) issuers, and did not specifically target investments by investment companies.<sup>13</sup>

This situation changed in 1980, when Section 3(c)(1) was amended to subject certain Section 3(c)(1) issuers<sup>14</sup> to all of the provisions of Section 12(d), which by that time had been amended to apply to fund of funds arrangements involving investments by unregistered investment companies in registered investment companies. As a result, investment by investment companies in certain Section 3(c)(1) issuers was subject to the Section 12(d)(1) restrictions, as was investment by such Section 3(c)(1) issuers in investment companies.

However, in 1992, the staff of the Commission's Division of Investment Management characterized the attribution provisions of Section 3(c)(1) as "overly broad" and recommended that Section 12(d)(1)'s fund of funds investment restrictions no longer apply to investments by registered investment companies in Section 3(c)(1) issuers.<sup>15</sup> In support of this recommendation, the staff noted that other provisions of the 1940 Act minimized the anti-pyramiding concerns underlying Section 12(d)(1) with respect to investments in such issuers, and specifically noted that the fiduciary duty provisions of Section 36 "could come into play where investments in [S]ection 3(c)(1) issuers result in unnecessary duplication of fees or expenses."<sup>16</sup> The staff anticipated that removal of the Section 12(d)(1) restrictions as applied to investment company investments in Section 3(c)(1) issuers would eliminate unnecessary constraints on such investments without compromising investor protection, and also would permit investment company investors to gain access to specialized investment services not otherwise offered by most investment companies.<sup>17</sup> However, the staff recommended that Section 3(c)(1) issuers still be limited with respect to their investments in registered funds in light of Section 12(d)(1)'s traditional concerns about undue influence over registered funds and disruption of portfolio management. In 1996, the staff's recommendations were implemented (including with respect to investments in Section 3(c)(7) issuers) as part of the National Securities Markets Improvement Act.

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<sup>13</sup> Specifically, the 10% limit was designed to prevent circumvention of the 100 investor limit contained in Section 3(c)(1) through layering of intermediaries. See Division of Investment Management, United States Securities and Exchange Commission, "Protecting Investors: A Half Century of Investment Company Regulation" (May 1992) (the "1992 Report") at 106.

<sup>14</sup> Essentially, these issuers were 3(c)(1) issuers with significant shareholders who were companies that did not otherwise significantly invest in Section 3(c)(1) issuers.

<sup>15</sup> 1992 Report at 105-110.

<sup>16</sup> *Id.* at 109 (emphasis added).

<sup>17</sup> *Id.*

The new disclosure requirements, as they apply to investments in Section 3(c)(1) and Section 3(c)(7) issuers, represent to some degree a reversal of these regulatory developments.<sup>18</sup> While we believe that this reversal is warranted in some cases, it is important that any new requirements be narrowly crafted to apply only to those types of issuers relying on Section 3(c)(1) or Section 3(c)(7) that raise genuine policy concerns. While the Commission has sought to protect fund investors from potential abuses arising from such an issuer's investment in an investment company, this goal is not furthered by blanket application of the new disclosure requirements to all issuers relying on Section 3(c)(1) or Section 3(c)(7).

*B. Traditional Fund of Funds Concerns Apply to Investments in Other Investment Companies, Not to Investments in Other Types of Issuers*

Historically, a number of considerations have justified regulation of funds of funds, including duplication of management, administrative, brokerage and sales commission fees, complex investment structures, diminution of investment performance due to the need to maintain a significant amount of fund assets in cash to honor redemption requests by a fund of funds, and the potential for funds of funds to influence management of an underlying fund to the detriment of the underlying fund's other shareholders.<sup>19</sup>

Of the concerns underpinning regulation of funds of funds, we believe that the most relevant to the disclosure requirements is the issue of duplicative fees, expenses and services. This concern was best highlighted by the Commission's 1966 Report concerning the growth of investment companies. In the 1966 Report, the Commission set forth three areas, in particular, in which funds of funds typically duplicated fees and expenses:<sup>20</sup>

- Advisory fees;

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<sup>18</sup> We believe that the Commission previously has recognized that investments by investment companies in such issuers do not significantly implicate investor protection concerns with respect to investors in registered investment companies. The restrictions that effectively limit investment by investment companies in such issuers have been implemented in order to ensure the private nature of issuers with a limited number of investors.

<sup>19</sup> See, e.g., SEC, *Public Policy Implications of Investment Company Growth*, reprinted in H.R. Rep. No. 89-2337 (Dec. 2, 1966) (the "1966 Report"). The 1966 Report expressed the Commission's concern in particular with the growth of Fund of Funds, Ltd., an unregistered Canadian open-end investment company that had gained a controlling stake in several U.S. registered mutual funds. As a result, Congress amended Section 12(d)(1) in 1970 to restrict an unregistered investment company's investments in registered investment companies.

<sup>20</sup> *Id.* at 318-19.

- Administrative expenses, which included stock transfer, dividend disbursement and custodial fees, as well as the cost of shareholder communications; and
- Sales loads, which were characterized as “acquisition expenses”.

The 1966 Report also noted that funds of funds may offer little in the way of diversification because many mutual funds may hold the same underlying securities and, perhaps, “one portfolio fund will be buying for its portfolio the same securities ... another will be selling, thereby subjecting the holding company’s overall assets to brokerage fees for what are, in effect, wash transactions ....”<sup>21</sup>

It is important to note that the Commission’s apparent concern was not the existence of fees and expenses associated with a fund’s investments, but rather the duplication of fees and expenses for the same type of services.<sup>22</sup> For example, the Commission does not require the disclosure by registered investment companies of the expenses of operating companies in which funds invest, even though operating companies may incur fees and expenses that are roughly analogous to management fees, administrative expenses and acquisition expenses. Nor has the Commission expressed interest in requiring operating expense disclosure with respect to investments in banks and insurance companies, which may be deemed to be more similar to registered investment companies than other operating companies because they rely on statutory exclusions from the “investment company” definition. We believe a similar approach is warranted with respect to many Section 3(c)(1) and Section 3(c)(7) issuers (specifically, operating company conduits and structured finance vehicles), as the recommendations contained in the 1992 Report reflect the Commission staff’s acknowledgement that investing in a Section 3(c)(1) issuer does not inherently raise the layering of fees and duplication of services concerns underpinning the Commission’s regulation of funds of funds.<sup>23</sup>

On the basis of the above, we believe that it is apparent that the Commission has demonstrated a lesser degree of concern regarding duplication of fees with respect to portfolio investments in entities that conduct activities and charge fees that are substantially different from registered funds. Accordingly, in regulating funds of funds, we believe that the staff of the Commission should be most concerned with actual duplication of services, fees and expenses (and not with services, fees and expenses that are roughly analogous but not duplicative), rather

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<sup>21</sup> *Id.* at 321.

<sup>22</sup> *Id.*

<sup>23</sup> Indeed, the staff noted that other sections of the 1940 Act could address any duplication that did occur, as the fiduciary duty provisions of Section 36 “could come into play where investments in [S]ection 3(c)(1) issuers result in unnecessary duplication of fees or expenses.” 1992 Report at 109 (emphasis added).

than on the specific statutory or regulatory provisions pursuant to which lower-tier vehicles operate.

As discussed in more detail below, operating company conduits and structured finance vehicles have operational features and fee structures that are significantly distinct from investment companies and Private Funds, and should not be deemed to raise the same regulatory concerns as traditional fund of funds arrangements.

*C. Application of the New Disclosure Requirements to Operating Company Conduits and Structured Finance Vehicles is Unnecessary*

In the release proposing the disclosure requirements, the Commission staff asked: "Is there a basis for treating disclosure of unregistered and registered fund expenses differently?" We believe that there is another relevant question: "Are all unregistered entities that make use of Sections 3(c)(1) or 3(c)(7) sufficiently similar to registered funds to make this fee disclosure useful?" We believe that limiting the application of the new disclosure requirements (as applicable to Section 3(c)(1) or 3(c)(7) issuers) to Private Funds captures the entities (e.g., hedge funds) that are sufficiently similar to investment companies to render the new disclosure requirements useful.

The new disclosure requirements cover a broad range of issuers that do not resemble traditional registered investment companies or Private Funds, do not pose the same type of potential management conflicts and do not duplicate fees and expenses of the type that the Commission traditionally has sought to regulate with respect to funds of funds. Rather, many of these entities more closely resemble entities to which the disclosure requirements have not been extended, such as operating companies, issuers of asset-backed securities that are able to rely on exclusions from the definition of "investment company" other than the Section 3(c)(1) or 3(c)(7) exclusions, and other issuers generally excluded from the 1940 Act's definition of investment company. Broadly, there are two general categories of entities that do not fit neatly into the new disclosure regime and for which disclosure of underlying operating expenses may not be useful to investors: (1) operating company conduits; and (2) structured finance vehicles.

*1. Operating Company Conduits*

This category includes entities that, rather than investing passively in the shares of operating companies, seek to participate in the management of operating companies or serve as incubators of actual operating companies. These entities include, but are not limited to, blank check companies, leveraged buy-out ("LBO") funds, and private equity funds. These entities do not resemble traditional registered investment companies, but do bear some superficial similarities to Private Funds. However, the Commission has recognized that these entities differ

in significant respects from Private Funds.<sup>24</sup> We believe that these differences make application of the new disclosure requirements to a registered investment company's investment in these entities inappropriate.

Unlike investment companies or Private Funds, operating company conduits generally require a long-term commitment of capital and are largely illiquid because they require more profound and sustained participation in the companies in which they invest. The continued existence of the underlying operating company may even depend on the funding and management of the operating company conduit. Further, unlike investors in an investment company or a Private Fund, who generally invest in the fund, at least in part, based on the investment adviser's advisory skills, ability or expertise, investors in operating company conduits typically evaluate the sponsor's ability to manage companies directly. Thus, while a Private Fund is typically a means by which to access the investment analysis and asset management skills of the sponsor, an operating company conduit is, to a much more significant extent, a means by which to gain access to the sponsor's ability to exercise influence over the management of portfolio investments. This difference generally will attract different types of investors, require different skill sets for management personnel, and give rise to significant differences in how these products are marketed. In addition, active portfolio management is not a characteristic of operating company conduits—the assets in a particular fund generally are largely static. Thus, despite being organized as entities that resemble Private Funds in certain respects and rely on the Section 3(c)(1) or 3(c)(7) exclusions, the actions carried out by these types of entities more closely resemble operating companies. Expenses and fees of operating company conduits may be inseparable from those of the underlying operating company - in the case of blank check companies, the entity itself becomes an operating company and any start-up operating expenses would be expensed as the operating company's operating expenses. Other fees are also qualitatively different from those of traditional investment companies or Private Funds. For example, broken-deal expenses and exit costs have no true analogues in traditional funds. Stock transfer, dividend disbursement and custodial fees (i.e., some of the potentially duplicative expenses highlighted in the 1966 Report) are rarely associated with operating company conduits.<sup>25</sup> As such, we do not believe that disclosure of fees of operating company conduits for the sake of comparison with fees of investment companies and/or Private Funds is useful, and may in fact be misleading. Further, the terms of operating company conduits with respect to fees, expenses and services are more variable than the terms of other types of funds.<sup>26</sup> As a result,

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<sup>24</sup> See, e.g., the discussion of Private Funds in the Hedge Fund Adviser Release.

<sup>25</sup> See gen. James M. Schell, Private Equity Funds Business Structure and Operations, (2006), at 2-1 – 2-40.

<sup>26</sup> Stephanie R. Breslow and Phyllis A. Schwartz, "Recent Trends in Private Equity Funds", Seventh Annual Private Equity Forum, (2006) at 3.

“apples to apples” comparisons of fees and expenses among even the same general type of operating company conduits can be difficult. Application of the new disclosure rules may present only the illusion of comparability, with the unintended effect of misleading investors.

Even to the extent that such entities resemble Private Funds in certain respects (e.g., reliance on the Section 3(c)(1) or Section 3(c)(7) exclusions), the Commission has not evidenced particular regulatory concern with respect to these entities because they do not have the same impact on listed companies or investors (particularly smaller investors) as Private Funds and do not raise comparable conflicts of interest posed by Private Funds (e.g., “side-by-side” management of client accounts or the relationships of hedge funds with prime brokers).<sup>27</sup>

The structure, fees and overall market impact of issuers in this general category do not raise the types of concerns that the Commission’s fund of funds regulation has sought to address, notwithstanding that some of them may rely on the Section 3(c)(1) or 3(c)(7) exclusions. We do not believe that comparison of the fees and expenses associated with an investment in these widely divergent entities with the fees and expense associated with an investment in Private Funds or investment companies will provide helpful information to investors in funds of funds. Accordingly, we believe that the application of the new disclosure requirements should be limited only to registered investment companies and Private Funds and should not extend to operating company conduits.

## 2. *Structured Finance Vehicles*

We also believe the new disclosure requirements should not apply to “structured finance vehicles” because such vehicles raise few of the concerns that warrant additional disclosure for investments in investment companies and Private Funds. Indeed, we understand that the Commission staff has informally acknowledged that the new disclosure rules were not meant to cover “structured finance products and collateralized debt obligations,” and indicated that the staff will not take action (through disclosure comments, inspection deficiency letters, or enforcement referrals) based on a registrant’s failure to reflect the fees and expenses of such entities in its fee table.<sup>28</sup> We request that the Commission formally adopt this position by revising

<sup>27</sup> Staff Report to the United States Securities and Exchange Commission, “Implications of the Growth of Hedge Funds” (September 2003) at 76, 79 and 83-85 (*avail. at* <http://www.sec.gov/news/studies/hedgelfunds0903.pdf>).

<sup>28</sup> Investment Company Institute, “SEC Staff Guidance on Definition of “Acquired Funds” in Fund of Funds Disclosure Rules,” December 19, 2006. Please note that some issuers may not be aware of this position if it is not more formally implemented. Furthermore, some issuers may not feel that they can rely on such informal guidance issued without the traditional imprimatur of the Commission or staff’s authority, namely implementation of the position through the rulemaking process or the publication of staff no-action positions.

the disclosure requirements as requested. In support of this request, we outline below certain key differences between structured finance vehicles, on one hand, and investment companies and Private Funds on the other, which justify application of the new disclosure rules only to investment companies and Private Funds.

A structured finance vehicle is a bankruptcy remote special purpose vehicle, organized as a corporation, partnership, limited liability company or trust, that typically issues multiple classes of non-redeemable securities that generally are rated debt securities whose performance depends primarily on the cash flows generated by an underlying pool of assets. As such, most structured finance vehicles differ substantially from both traditional investment companies and Private Funds with respect to their operations and fees and expenses. The Commission's Division of Investment Management has pointed out significant differences between structured finance vehicles and investment companies: "[T]he purpose of structured finance is quite different from that of most investment companies. Structured finance primarily is a financing technique that integrates the capital markets with borrowers seeking access to those markets; the sponsors of asset securitizations are seeking a source of financing. In contrast, investment companies are intended to provide the advantages of professional management, diversification, and economies of scale to investors."<sup>29</sup> The Commission staff also recognized that, unlike Private Funds, structured finance vehicles' unique characteristics tend to limit potential opportunities for abuses, to wit: (i) most structured finance securities are sold to institutional investors with a high degree of financial sophistication; (ii) most structured financings are subject to strict conditions imposed by the rating agencies that they be structured to minimize the chance that investors in the rated securities will receive less than full and timely payment; and (iii) most sponsors of structured financings are large, well-known companies.<sup>30</sup>

In addition, we note that structured finance vehicles typically differ from most investment companies and Private Funds in several other significant respects. First, a primary purpose of a structured finance vehicle is arbitrage - the creation of multiple classes of rated senior/subordinate securities with different maturities, interest rates and payment characteristics to attract investors with different investment requirements and appetites in the market.<sup>31</sup> Second, structured finance

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<sup>29</sup> 1992 Report at 76-77.

<sup>30</sup> *Id.* at 81-82.

<sup>31</sup> As pointed out in the 1992 Report, "[t]he yields paid to investors [in structured finance securities] obviously must be lower than the effective yield on the underlying assets" because "[i]nvestors, in effect, give up a substantial portion of the yield spread because the transformation of these assets into securities enables investors to receive what they consider to be safer and more liquid investments than if they had purchased the assets without the financing being structured." *Id.* at 33.

vehicles generally issue non-redeemable securities.<sup>32</sup> Third, fees paid are, in significant part, to safeguard the assets that produce the cash flow for the securities issued by the structured finance vehicle.<sup>33</sup> In comparison, a Private Fund (and most investment companies) typically issues redeemable securities to investors who intend not to invest in fixed income securities in a rated transaction the payment of which is primarily dependent on the cash flow from a pool of assets, but rather to invest in an investment fund based on the investment strategy outlined in the fund's offering documents which typically includes market gain as part of the strategy and the expertise of the investment manager whose interests are aligned with the fund investors by tying fees to net asset value calculations.

Since structured finance vehicles do not closely resemble registered funds or Private Funds, and because an investment in securities issued by a structured finance vehicle does not raise the same policy concerns of duplicative fees and expenses as an investment in investment companies or Private Funds,<sup>34</sup> we believe that the new disclosure requirements should not apply to structured finance vehicles.

### **III. Proposed Rules Relating to the Disclosure of Fund of Funds Investments**

#### *A. Regulatory Authority*

We believe that the Commission has the authority under existing law to amend the operating expense disclosure for unregistered entities that are not Private Funds. Section 6(c) of the 1940 Act provides:

The Commission, by rule or regulations upon its own motion, or by order upon application, may conditionally or unconditionally exempt any person, securities, or transaction, or any class or classes of persons, securities, or transactions, from any provision or provisions of this title or of any rule or regulation thereunder, if and to the extent that such exemption is necessary or appropriate in the public

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<sup>32</sup> However, one or more classes of investors typically may cause the issuer to redeem all of the issuer's securities in connection with the sale of assets of the issuer and liquidation of the vehicle, or in connection with a refinancing of the issuer's debt securities.

<sup>33</sup> For structured finance vehicles, fees are typically paid as a relatively small market-driven percentage of assets under management measured at par (subject to a discount for defaulted assets).

<sup>34</sup> See Tamar Frankel, Securitization: Structured Financing, Financial Assets Pools, and Asset-Backed Securities, 2ed. (2005) at 606.

interest, and consistent with the protection of investors and the purposes fairly intended by the policy and provisions of this title.

We are petitioning the Commission to amend the disclosure requirements pursuant to Section 6(c) because we believe that seeking no-action relief for each Fidelity fund's investment in a Section 3(c)(1) or 3(c)(7) issuer that is not a Private Fund is not a viable alternative. Further, we believe that a legislative solution is not feasible in the foreseeable future.

For the reasons discussed above, we believe that the proposed amendments to the disclosure requirements are appropriate in the public interest and consistent with the protection of investors. As currently drafted, the disclosure requirements are overly inclusive, and require registrants to reflect in their operating expenses the expenses and fees of issuers that are not particularly comparable to investment companies and which do not typically raise the type of concerns regarding duplication of services, fees and expenses as arrangements that traditionally have been regulated by Section 12(d)(1), notwithstanding the fact that they rely on exclusions commonly relied upon by Private Funds. We believe that the disclosure will be most meaningful to investors if it is limited to issuers of the type that the Commission traditionally has focused on when regulating funds of funds.

We attach proposed amendments to various investment company registration statement forms that reflect the proposed disclosure requirements discussed above. The core principle embodied in the proposed amendments is that certain entities differ substantially from traditional investment companies and unregistered investment funds. With respect to operating company conduits, the primary differences arise because their structures closely resemble or are complementary to those of the operating companies. For structured finance vehicles, the primary differences arise because the structure serves primarily to provide a bankruptcy-remote vehicle for certain assets to facilitate a financing transaction. The fees and expenses of these entities are not significantly duplicative of the fees and expenses typically associated with registered investment companies, and the services provided by their sponsors are qualitatively different from those typically associated with registered investment companies or Private Funds. Because of these critical differences, registered investment companies should not have to discover and disclose the operating expenses associated with these types of entities.

*B. Proposed Rule Changes*

We propose that the disclosure requirements extend only to investments in lower-tier funds that are "investment companies" or "private funds" as defined in former Investment

Advisers Act Rule 203(b)(3)-1(d).<sup>35</sup> Please see attached Appendix A for the text of the proposed amended disclosure requirements for Forms N-1A, N-2, N-3, N-4 and N-6.

#### **IV. Conclusion**

For the reasons set forth above, we believe that the disclosure requirements as adopted in the Fund of Funds Release are overly broad and require disclosure of the fees and expenses associated with investments in issuers that are beyond the scope of the Commission's traditional concerns with respect to funds of funds, notwithstanding the fact that these issuers may rely on the same exclusions as those relied upon by unregistered investment funds. As drafted, the requirements may impose burdens on registered investment companies that must comply with the requirements, and impose somewhat arbitrary distinctions between certain issuers that rely on Sections 3(c)(1) or 3(c)(7) and comparable issuers that are able to rely on other exclusions from the definition of investment company. As a result, this disclosure, as it relates to investments in certain Sections 3(c)(1) or 3(c)(7) issuers, is unlikely to provide meaningful information to investors, while doing so at a considerable burden to registrants. Accordingly, we request that the

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<sup>35</sup> The exception from the definition of "private fund" provided to regulated offshore funds in former Rule 203(b)(3)-1(d)(3) is not included in the proposed disclosure requirements, as such issuers likely would be deemed to be "investment companies".

disclosure requirements applicable to a registered investment company's investments in issuers relying on Sections 3(c)(1) or 3(c)(7) be limited to those issuers that qualify as Private Funds.

Thank you for your consideration of this petition. If you need additional information, please contact Stephen Fisher at (617) 563-7139.

Very truly yours,



Stephen Fisher  
Senior Vice President and  
Deputy General Counsel  
Fidelity Management &  
Research Company

*Eric D. Roiter /SDF*

Eric Roiter  
Senior Vice President and  
General Counsel  
Fidelity Management &  
Research Company

Attachment

cc: Chairman Christopher Cox  
Commissioner Paul S. Atkins  
Commissioner Roel C. Campos  
Commissioner Kathleen L. Casey  
Commissioner Annette L. Nazareth  
Andrew J. Donohue, Director, Division of Investment Management  
Robert E. Plaze, Associate Director, Division of Investment Management  
Barry D. Miller, Associate Director, Division of Investment Management  
Penelope W. Saltzman, Branch Chief, Office of Regulatory Policy, Division of  
Investment Management



## APPENDIX A

### Form N-1A

Form N-1A, Item 3, would be amended by modifying paragraph (f) to Instruction 3 to read as follows:

#### Item 3. Risk/Return Summary: Fee Table

\* \* \* \* \*

*Instructions*

\* \* \* \* \*

3. *Annual Fund Operating Expenses.*

\* \* \* \* \*

(f)(i) If the Fund (unless it is a Feeder Fund) invests in shares of one or more Acquired Funds, add a subcaption to the "Annual Fund Operating Expenses" portion of the table directly above the subcaption titled "Total Annual Fund Operating Expenses." Title the additional subcaption: "Acquired Fund Fees and Expenses." Disclose in the subcaption fees and expenses incurred indirectly by the Fund as a result of investment in shares of one or more Acquired Funds. For purposes of this item, an "Acquired Fund" means any company in which the Fund invests or has invested during the relevant fiscal period that (A) is an investment company or (B) ~~would be an investment company under section 3(a) of the Investment Company Act (15 U.S.C. 80a-3(a)) but for the exceptions to that definition provided for in sections 3(c)(1) and 3(c)(7) of the Investment Company Act (15 U.S.C. 80a-3(c)(1) and 80a-3(c)(7))~~ is a Private Fund. A Private Fund is a company: (i) That would be an investment company under section 3(a) of the Investment Company Act of 1940 (15 U.S.C. 80a-3(a)) but for the exception provided from that definition by either section 3(c)(1) or section 3(c)(7) of such Act (15 U.S.C. 80a-3(c)(1) or (7)); (ii) That permits its owners to redeem any portion of their ownership interests within two years of the purchase of such interests; and (iii) Interests in which are or have been offered based on the investment advisory skills, ability or expertise of the investment adviser. Notwithstanding the above, a company is not a Private Fund if it permits its owners to redeem their ownership interests within two years of the purchase of such interests only in the case of: (i) Events determined after reasonable inquiry to be extraordinary; and (ii) Interests acquired through reinvestment of distributed capital gains or income. If a Fund uses another term in response to other requirements of this Form to refer to Acquired Funds, it may include that term in parentheses following the subcaption title. In the event the fees and expenses

by the Fund as a result of investment in shares of one or more Acquired Funds do not exceed 0.01 percent (one basis point) of average net assets of the Fund, the Fund may include these fees and expenses under the subcaption "Other Expenses" in lieu of this disclosure requirement.

(ii) Determine the "Acquired Fund Fees and Expenses" according to the following formula:

$$\text{AFFE} = \frac{[(F1/FY)*AI1 * D1] + [(F2/FY)*AI2 * D2] + [(F3/FY)*AI3 * D3]}{\text{Average Net Assets of the Fund}} + \text{Transaction Fees} + \text{Incentive Allocations}$$

Average Net Assets of the Fund

Where:

AFFE = Acquired Fund fees and expenses;

$F_1, F_2, F_3, \dots$  = Total annual operating expense ratio for each Acquired Fund;

FY = Number of days in the relevant fiscal year.

$AI_1, AI_2, AI_3, \dots$  = Average invested balance in each Acquired Fund;

$D_1, D_2, D_3, \dots$  = Number of days invested in each Acquired Fund; and

"Transaction Fees" = The total amount of sales loads, redemption fees, or other transaction fees paid by the Fund in connection with acquiring or disposing of shares in any Acquired Funds during the most recent fiscal year.

"Incentive Allocations" = Any allocation of capital from the Acquiring Fund to the adviser of the Acquired Fund (or its affiliate) based on a percentage of the Acquiring Fund's income, capital gains and/or appreciation in the Acquired Fund.

(iii) Calculate the average net assets of the Fund for the most recent fiscal year, as provided in Item 8(a) (see Instruction 4 to Item 8(a)).

(iv) The total annual operating expense ratio used for purposes of this calculation ( $F_1$ ) is the annualized ratio of operating expenses to average net assets for the Acquired Fund's most recent fiscal period as disclosed in the Acquired Fund's most recent shareholder report. If the ratio of expenses to average net assets is not included in the most recent shareholder report or the Acquired Fund is a newly formed fund that has not provided a shareholder report, then the ratio of expenses to average net assets of the Acquired Fund is the ratio of total annual operating expenses to average annual net assets of the Acquired Fund for its most recent fiscal period as disclosed in the most recent communication from the Acquired Fund to the Fund. For purposes of this instruction: (i) Acquired Fund expenses include increases resulting from brokerage service and expense offset arrangements and reductions resulting from fee waivers or reimbursements by the Acquired Funds' investment advisers or sponsors; and (ii) Acquired Fund expenses do not include expenses (i.e., performance fees) that are incurred solely upon the realization and/or distribution of a gain. If an Acquired Fund has no operating history, include in the Acquired Funds' expenses any fees payable to the Acquired Fund's investment adviser or its affiliates

stated in the Acquired Fund's registration statement, offering memorandum or other similar communication without giving effect to any performance.

(v) To determine the average invested balance (AI), the numerator is the sum of the amount initially invested in an Acquired Fund during the most recent fiscal year (if the investment was held at the end of the previous fiscal year, use the amount invested as of the end of the previous fiscal year) and the amounts invested in the Acquired Fund no less frequently than monthly during the period the investment is held by the Fund (if the investment was held through the end of the fiscal year, use each month-end through and including the fiscal year-end). Divide the numerator by the number of measurement points included in the calculation of the numerator (*i.e.*, if an investment is made during the fiscal year and held for 3 succeeding months, the denominator would be 4).

(vi) A New Fund should base the Acquired Fund fees and expenses on assumptions as to the specific Acquired Funds in which the New Fund expects to invest. Disclose in a footnote to the table that Acquired Fund fees and expenses are based on estimated amounts for the current fiscal year.

(vii) The Fund may clarify in a footnote to the fee table that the total annual fund operating expenses under Item 3 do not correlate to the ratio of expenses to average net assets given in response to Item 8, which reflects the operating expenses of the Fund and does not include Acquired Fund fees and expenses.

## Form N-2

Form N-2, Item 3, would be amended by modifying paragraphs (10)(a) and (10)(h) to Instruction 3 to read as follows:

\* \* \* \* \*

### Item 3. Fee Table and Synopsis

1. \* \* \*

*Instructions:*

\* \* \* \* \*

10. a. If the Registrant invests, or intends to invest based upon the anticipated net proceeds of the present offering, in shares of one or more "Acquired Funds," add a subcaption to the "Annual Expenses" portion of the table directly above the subcaption titled "Total Annual Expenses." Title the additional subcaption: "Acquired Fund Fees and Expenses." Disclose in the subcaption fees and expenses incurred indirectly by the Registrant as a result of investment in shares of one or more Acquired Funds. For purposes of this item, an "Acquired Fund" means any company in which the Registrant invests or intends to invest that (A) that is an investment company or (B) that would be an investment company under section 3(a) of the 1940 Act (15 U.S.C. 80a-3(a)) but for the exceptions to that definition provided for in sections 3(c)(1) and 3(c)(7) of the 1940 Act (15 U.S.C. 80a-3(c)(1) and 80a-3(c)(7)) is a Private Fund. A Private Fund is a company: (i) That would be an investment company under section 3(a) of the Investment Company Act of 1940 (15 U.S.C. 80a-3(a)) but for the exception provided from that definition by either section 3(c)(1) or section 3(c)(7) of such Act (15 U.S.C. 80a-3(c)(1) or (7)); (ii) That permits its owners to redeem any portion of their ownership interests within two years of the purchase of such interests; and (iii) Interests in which are or have been offered based on the investment advisory skills, ability or expertise of the investment adviser. Notwithstanding the above, a company is not a Private Fund if it permits its owners to redeem their ownership interests within two years of the purchase of such interests only in the case of: (i) Events determined after reasonable inquiry to be extraordinary; and (ii) Interests acquired through reinvestment of distributed capital gains or income. If a Registrant uses another term in response to other requirements of this Form to refer to Acquired Funds, it may include that term in parentheses following the subcaption title. In the event the fees and expenses incurred indirectly by the Registrant as a result of investment in shares of one or more Acquired Funds do not exceed 0.01 percent (one basis point) of average net assets of the Registrant, the Registrant may include these fees and expenses under the subcaption "Other Expenses" in lieu of this disclosure requirement.

b. Determine the "Acquired Fund Fees and Expenses" according to the following formula:

$$\text{AFFE} = \frac{[(F1/\text{FY}) * \text{AI1} * D1] + [(F2/\text{FY}) * \text{AI2} * D2] + [(F3/\text{FY}) * \text{AI3} * D3]}{\text{Average Net Assets of the Registrant}} + \text{Transaction Fees} + \text{Incentive Allocations}$$

Average Net Assets of the Registrant

Where:

AFFE = Acquired Fund fees and expenses;

F1, F2, F3, . . . = Total annual operating expense ratio for each Acquired Fund;

FY = Number of days in the relevant fiscal year.

AI1, AI2, AI3, . . . = Average invested balance in each Acquired Fund;

D1, D2, D3, . . . = Number of days invested in each Acquired Fund;

"Transaction Fees" = The total amount of sales loads, redemption fees, or other transaction fees paid by the Registrant in connection with acquiring or disposing of shares in any Acquired Funds during the most recent fiscal year; and

"Incentive Allocations" = Any allocation of capital from the Acquiring Fund to the adviser of the Acquired Fund (or its affiliate) based on a percentage of the Acquiring Fund's income, capital gains and/or appreciation in the Acquired Fund.

c. Calculate the average net assets of the Registrant for the most recent fiscal year, as provided in Item 4.1 (see Instruction 15 to Item 4.1) and include the anticipated net proceeds of the present offering.

d. The total annual operating expense ratio used for purposes of this calculation (F1) is the annualized ratio of operating expenses to average net assets for the Acquired Fund's most recent fiscal period as disclosed in the Acquired Fund's most recent shareholder report. If the ratio of expenses to average net assets is not included in the most recent shareholder report or the Acquired Fund is a newly formed fund that has not provided a shareholder report, then the ratio of expenses to average net assets of the Acquired Fund is the ratio of total annual operating expenses to average annual net assets of the Acquired Fund for its most recent fiscal period as disclosed in the most recent communication from the Acquired Fund to the Registrant. If the Registrant has a written fee agreement with the Acquired Fund that would affect the ratio of expenses to average net assets as disclosed in the Acquired Fund's most recent shareholder report, the Registrant should determine the ratio of expenses to average net assets for the Acquired Fund's most recent fiscal period using the written fee agreement. For purposes of this instruction: (i) Acquired Fund expenses include increases resulting from brokerage service and expense offset arrangements and reductions resulting from fee waivers or reimbursements by the Acquired Funds' investment advisers or sponsors; and (ii) Acquired Fund expenses do not include any expenses (i.e., performance fees) that are calculated solely upon the realization and/or

distribution of gains, or the sum of the realization and/or distribution of gains and unrealized appreciation of assets distributed in-kind. If an Acquired Fund has no operating history, include in the Acquired Funds' expenses any fees payable to the Acquired Fund's investment adviser or its affiliates stated in the Acquired Fund's registration statement, offering memorandum or other similar communication without giving effect to any performance.

e. If a Registrant has made investments in the most recent fiscal year, to determine the average invested balance (AII), the numerator is the sum of the amount initially invested in an Acquired Fund during the most recent fiscal year (if the investment was held at the end of the previous fiscal year, use the amount invested as of the end of the previous fiscal year) and the amounts invested in the Acquired Fund no less frequently than monthly during the period the investment is held by the Registrant (if the investment was held through the end of the fiscal year, use each month-end through and including the fiscal year-end). Divide the numerator by the number of measurement points included in the calculation of the numerator (i.e., if an investment is made during the fiscal year and held for 3 succeeding months, the denominator would be 4).

f. For investments based upon the anticipated net proceeds from the present offering, base the "Acquired Fund Fees and Expenses" on: (i) assumptions about specific funds in which the Registrant expects to invest, (ii) estimates of the amount of assets the Registrant expects to invest in each of those Acquired Funds, and (iii) an assumption that the investment was held for all of the Registrant's most recent fiscal year and was subject to the Acquired Funds' fees and expenses for that year. Disclose in a footnote to the table that Acquired Fund fees and expenses are based on estimated amounts for the current fiscal year.

g. If an Acquired Fund charges an Incentive Allocation or any other fee based on income, capital gains and/or appreciation (i.e., performance fee), the Registrant must include a footnote to the "Acquired Fund Fees and Expenses" subcaption that: (i) discloses the typical Incentive Allocation or such other fee (expressed as a percentage) to be paid to the investment advisers of the Acquired Funds (or an affiliate); (ii) discloses that Acquired Funds' fees and expenses are based on historic fees and expenses; and (iii) states that future Acquired Funds' fees and expenses may be substantially higher or lower because certain fees are based on the performance of the Acquired Funds, which may fluctuate over time.

h. If the Registrant is a Feeder Fund, reflect the aggregate expenses of the Feeder Fund and the Master Fund in the "Acquired Fund Fees and Expenses." The aggregate expenses of the Master-Feeder Fund must include the fees and expenses incurred indirectly by the Feeder Fund as a result of the Master Fund's investment in shares of one or more companies (A) that are investment companies or (B) that ~~would be investment companies under section 3(a) of the 1940 Act (15 U.S.C. 80a-3(a)) but for the exceptions to that definition provided for in sections 3(c)(1) and 3(c)(7) of the 1940 Act (15 U.S.C. 80a-3(c)(1) and 80a-3(c)(7))~~ are Private Funds. A Private Fund is a company: (i) That would be an investment company under section 3(a) of the Investment Company Act of 1940 (15 U.S.C. 80a-3(a)) but for the exception provided from that definition by either section 3(c)(1) or section 3(c)(7) of such Act (15 U.S.C. 80a-3(c)(1) or (7));

(ii) That permits its owners to redeem any portion of their ownership interests within two years of the purchase of such interests; and (iii) Interests in which are or have been offered based on the investment advisory skills, ability or expertise of the investment adviser. Notwithstanding the above, a company is not a Private Fund if it permits its owners to redeem their ownership interests within two years of the purchase of such interests only in the case of: (i) Events determined after reasonable inquiry to be extraordinary; and (ii) Interests acquired through reinvestment of distributed capital gains or income. For purposes of this instruction, a “Master-Feeder Fund” means a two-tiered arrangement in which one or more investment companies registered under the 1940 Act (each a “Feeder Fund”) holds shares of a single management investment company registered under the 1940 Act (the “Master Fund”) in accordance with section 12(d)(1)(E) of the 1940 Act [15 U.S.C. 80a-12(d)(1)(E)].

i. The Registrant may clarify in a footnote to the fee table that the total annual expenses item under Item 3.1 is different from the ratio of expenses to average net assets given in response to Item 4.1, which reflects the operating expenses of the Registrant and does not include Acquired Fund fees and expenses.

**Form N-3**

Form N-3, Item 3, would be amended by modifying paragraph (19)(a) to the Instructions to read as follows:

\* \* \* \* \*

\* \* \* \* \*

**Item 3. Synopsis or Highlights**

(a) \* \* \*

*Instructions:*

\* \* \* \* \*

19. (a) If the Registrant invests in shares of one or more Acquired Funds, add a subcaption to the "Annual Expenses" portion of the table directly above the subcaption titled "Total Annual Expenses." Title the additional subcaption: "Acquired Fund Fees and Expenses." Disclose in the subcaption fees and expenses incurred indirectly by the Registrant as a result of investment in shares of one or more Acquired Funds. For purposes of this Item, an "Acquired Fund" means any company in which the Fund invests that (i) is an investment company or (ii) ~~would be an investment company under section 3(a) of the 1940 Act (15 U.S.C. 80a-3(a)) but for the exceptions to that definition provided for in sections 3(c)(1) and 3(c)(7) of the 1940 Act (15 U.S.C. 80a-3(c)(1) and 80a-3(c)(7))~~ is a Private Fund. A Private Fund is a company: (i) That would be an investment company under section 3(a) of the Investment Company Act of 1940 (15 U.S.C. 80a-3(a)) but for the exception provided from that definition by either section 3(c)(1) or section 3(c)(7) of such Act (15 U.S.C. 80a-3(c)(1) or (7)); (ii) That permits its owners to redeem any portion of their ownership interests within two years of the purchase of such interests; and (iii) Interests in which are or have been offered based on the investment advisory skills, ability or expertise of the investment adviser. Notwithstanding the above, a company is not a Private Fund if it permits its owners to redeem their ownership interests within two years of the purchase of such interests only in the case of: (i) Events determined after reasonable inquiry to be extraordinary; and (ii) Interests acquired through reinvestment of distributed capital gains or income. If a Registrant uses another term in response to other requirements of this Form to refer to Acquired Funds, it may include that term in parentheses following the subcaption title. In the event the fees and expenses incurred indirectly by the Registrant as a result of investment in shares of one or more Acquired Funds do not exceed 0.01 percent (one basis point) of average net assets of the Registrant, the Registrant may include these fees and expenses under the subcaption "Other Expenses" in lieu of this disclosure requirement.

(b) Determine the "Acquired Fund Fees and Expenses" according to the following formula:

$$\text{AFFE} = [(F1/FY)*AI1* D1]+[(F2/FY)*AI2* D2]+[(F3/FY)*AI3* D3] + \text{Transaction Fees}$$

Average Net Assets of the Fund

Where:

AFFE = Acquired Fund fees and expenses;

F1, F2, F3, . . . = Total annual operating expense ratio for each Acquired Fund;

FY = Number of days in the relevant fiscal year.

AI1, AI2, AI3, . . . = Average invested balance in each Acquired Fund;

D1, D2, D3, . . . = Number of days invested in each Acquired Fund; and

“Transaction Fees” = The total amount of sales loads, redemption fees, or other transaction fees paid by the Registrant in connection with acquiring or disposing of shares in any Acquired Funds during the most recent fiscal year.

(c) Calculate the average net assets of the Registrant for the most recent fiscal year, as provided in Item 4(a) (see Instruction 10 to Item 4(a)).

(d) The total annual operating expense ratio used for purposes of this calculation (F1) is the annualized ratio of operating expenses to average net assets for the Acquired Fund’s most recent fiscal period as disclosed in the Acquired Fund’s most recent shareholder report. If the ratio of expenses to average net assets is not included in the most recent shareholder report or the Acquired Fund is a newly formed fund that has not provided a shareholder report, then the ratio of expenses to average net assets of the Acquired Fund is the ratio of total annual operating expenses to average annual net assets of the Acquired Fund for its most recent fiscal period as disclosed in the most recent communication from the Acquired Fund to the Registrant. For purposes of this instruction, Acquired Fund expenses include increases resulting from brokerage service and expense offset arrangements and reductions resulting from fee waivers or reimbursements by the Acquired Funds’ investment advisers or sponsors.

(e) To determine the average invested balance (AI1), the numerator is the sum of the amount initially invested in an Acquired Fund during the most recent fiscal year (if the investment was held at the end of the previous fiscal year, use the amount invested as of the end of the previous fiscal year) and the amounts invested in the Acquired Fund no less frequently than monthly during the period the investment is held by the Registrant (if the investment was held through the end of the fiscal year, use each month-end through and including the fiscal year-end). Divide the numerator by the number of measurement points included in the calculation of the numerator (i.e., if an investment is made during the fiscal year and held for 3 succeeding months, the denominator would be 4).

(f) A New Registrant should base the “Acquired Fund Fees and Expenses” on assumptions as to the specific Acquired Funds in which the New Registrant expects to invest. Disclose in a footnote to the table that Acquired Fund fees and expenses are based on estimated amounts for the current fiscal year.

(g) The Registrant may clarify in a footnote to the fee table that the total annual expenses under Item 3 are different from the ratio of expenses to average net assets given in response to Item 4, which reflects the operating expenses of the Registrant and does not include Acquired Fund fees and expenses.

**Form N-4**

Form N-4, Item 3, would be amended by modifying paragraph (17)(a) to the Instructions to read as follows:

\* \* \* \* \*

**Item 3. Synopsis**

\* \* \* \* \*

*Instructions:*

\* \* \* \* \*

17. (a) \* \* \* If any Portfolio Company invests in shares of one or more Acquired Funds, "Total Annual [Portfolio Company] Operating Expenses" for the Portfolio Company must also include fees and expenses incurred indirectly by the Portfolio Company as a result of investment in shares of one or more Acquired Funds, calculated in accordance with Instruction 3(f) to Item 3 of Form N-1A (17 CFR 239.15A; 17 CFR 274.11A). For purposes of this paragraph, an Acquired Fund means any company in which the Portfolio Company invests that (i) is an investment company or (ii) ~~would be an investment company under section 3(a) of the 1940 Act (15 U.S.C. 80a-3(a)) but for the exceptions to that definition provided for in sections 3(c)(1) and 3(c)(7) of the 1940 Act (15 U.S.C. 80a-3(c)(1) and 80a-3(c)(7))~~ is a Private Fund. A Private Fund is a company: (i) That would be an investment company under section 3(a) of the Investment Company Act of 1940 (15 U.S.C. 80a-3(a)) but for the exception provided from that definition by either section 3(c)(1) or section 3(c)(7) of such Act (15 U.S.C. 80a-3(c)(1) or (7)); (ii) That permits its owners to redeem any portion of their ownership interests within two years of the purchase of such interests; and (iii) Interests in which are or have been offered based on the investment advisory skills, ability or expertise of the investment adviser. Notwithstanding the above, a company is not a Private Fund if it permits its owners to redeem their ownership interests within two years of the purchase of such interests only in the case of: (i) Events determined after reasonable inquiry to be extraordinary; and (ii) Interests acquired through reinvestment of distributed capital gains or income.

**Form N-6**

Form N-6, Item 3, would be amended by modifying paragraph (4)(b) to the Instructions to read as follows:

\* \* \* \* \*

**Item 3. Risk/Benefit Summary: Fee Table**

\* \* \* \* \*

*Instructions:*

\* \* \* \* \*

**4. Total Annual [Portfolio Company] Operating Expenses.**

\* \* \* \* \*

(b) \* \* \* If any Portfolio Company invests in shares of one or more Acquired Funds, "Total Annual [Portfolio Company] Operating Expenses" for the Portfolio Company must also include fees and expenses incurred indirectly by the Portfolio Company as a result of investment in shares of one or more Acquired Funds, calculated in accordance with Instruction 3(f) to Item 3 of Form N-1A (17 CFR 239.15A; 17 CFR 274.11A). For purposes of this paragraph, an Acquired Fund means any company in which the Portfolio Company invests that (i) is an investment company or (ii) ~~would be an investment company under section 3(a) of the Investment Company Act (15 U.S.C. 80a-3(a)) but for the exceptions to that definition provided for in sections 3(e)(1) and 3(e)(7) of the Investment Company Act (15 U.S.C. 80a-3(e)(1) and 80a-3(e)(7))~~ is a Private Fund. A Private Fund is a company: (i) That would be an investment company under section 3(a) of the Investment Company Act of 1940 (15 U.S.C. 80a-3(a)) but for the exception provided from that definition by either section 3(c)(1) or section 3(c)(7) of such Act (15 U.S.C. 80a-3(c)(1) or (7)); (ii) That permits its owners to redeem any portion of their ownership interests within two years of the purchase of such interests; and (iii) Interests in which are or have been offered based on the investment advisory skills, ability or expertise of the investment adviser. Notwithstanding the above, a company is not a Private Fund if it permits its owners to redeem their ownership interests within two years of the purchase of such interests only in the case of: (i) Events determined after reasonable inquiry to be extraordinary; and (ii) Interests acquired through reinvestment of distributed capital gains or income.