The following summarizes recent legal developments of note affecting the mutual fund/investment management industry:

SEC Proposes New Short Form Prospectus Requirements

On November 15, 2007, the SEC voted to propose amendments to Form N-1A as part of an effort to enhance the disclosures provided to mutual fund investors. The form amendments would require every prospectus to include a summary section at the front of the prospectus consisting of key information about the fund, including investment objectives and strategies, risks, costs, and performance. This key information would be required to be presented in plain English in a standardized order, and a separate summary section would be presented for each fund covered by a multiple fund prospectus.

The SEC is also proposing rule amendments that would permit a person to satisfy its mutual fund prospectus delivery obligations under Section 5(b)(2) of the Securities Act of 1933 by sending or giving the key information directly to investors in the form of a summary prospectus and providing the statutory prospectus on an Internet Web site. Under the proposed rules, key information could be sent or given to investors in the form of a summary prospectus, provided that the statutory prospectus, statement of additional information and most recent shareholder reports were available on an Internet Web site in a format allowing investors to effectively use the detailed information. Upon an investor's request, funds would also be required to send the statutory prospectus and other information in paper form to an investor within three days of the request. Failure to provide a hard copy of the statutory prospectus to the investor within three days would constitute a rule violation but would not invalidate the prospectus delivery for liability purposes.

ICI and IDC Publish Update on Fund Governance Practices

The Investment Company Institute ("ICI") and The Independent Directors Council ("IDC") have jointly issued a study, *Overview of Fund Governance Practices, 1994-2006* ("2007 Overview"), which updates previous ICI/IDC studies to include its most recent survey of industry data covering the period through the end of 2006. Among the key findings noted in the 2007 Overview is that the percentage of complexes with at least 75 percent independent directors increased from 52 percent in 2000 to 88 percent in 2006. The percentage of complexes having independent lead directors also increased, rising from 18 percent in 2004 to 24 percent by the end of 2006, and the percentage of complexes having an independent chair increased from 43 percent in 2004 to 56 percent by 2006. The number of fund complexes for which the independent directors are represented by independent counsel has also increased, with more than nine out of 10 fund complexes currently having such representation. Despite the fact that there is no formal regulatory requirement to do so, 94 percent of complexes have an audit committee financial expert serving on the audit committee. Survey data concerning directors' ownership of fund shares indicate that 23 percent of participating complexes now require fund share ownership by their directors, and another 38 percent encourage it. The 2007 Overview reports that voluntary adoption of mandatory retirement policies has increased, with about 63 percent of complexes having formally adopted mandatory retirement policies. Of the complexes with policies for mandatory retirement, the average mandatory retirement age is between 72 and 73 years old over the 10-year period from 1996-2006.

Massachusetts Secretary of State Files Enforcement Action against Bear Stearns

On November 14, 2007, the Massachusetts Secretary of State's office filed an administrative complaint against Bear Stearns Asset Management ("BSAM") alleging that BSAM violated the Massachusetts Uniform Securities Act by failing to follow proper procedures regarding the approval of principal trades and other transactions involving conflicts of interests between affiliates of Bear Stearns and the investors in two funds advised by BSAM. These funds, which invested in collateralized

debt obligations, became insolvent during the recent sub-prime lending crisis and filed for bankruptcy in the summer of 2007. The complaint alleges that the two funds bought and sold securities from a Bear Stearns affiliated broker-dealer and from investment vehicles structured by the funds' investment managers. As described in their offering documents, the funds' operating procedures and Rule 206(3) of the Investment Advisers Act required pre-trade disclosure to, and approval of, the funds' unaffiliated directors. According to the complaint, a high percentage of relevant transactions did not receive prior approval from the unaffiliated directors. The Secretary of State alleges that BSAM staff responsible for obtaining the requisite approvals did not receive adequate training; did not understand the importance of the approvals; and were unaware that failure to obtain the approvals was a violation of federal law and of the Funds' offering documents. The complaint alleges that (i) the failure to obtain consent from unaffiliated directors and (ii) continued offer to sell interests in the funds under offering documents that contained a procedure which BSAM senior management knew was not being followed, constitute untrue statements of material fact under the Massachusetts Uniform Securities Act. The Secretary of State requests that BSAM be censured; ordered to permanently cease and desist from violating relevant Massachusetts law; and required to pay an administrative fine.

SEC Staff Allows Affiliate Letter of Credit to Replace Downgraded Notes in Money Market Fund

In recent no-action letters, the SEC provided relief under Sections 12(d)(3), 17(a) and 17(d) of the Investment Company Act of 1940 to allow money market funds to treat certain types of "capital support" provided by the fund's adviser (or the adviser's parent) as an "Eligible Security" as defined in under Rule 2a-7 of the Investment Company Act. The need for the no-action letter requests arose when the credit ratings of certain notes held by the money market funds were downgraded below the credit rating required for the notes to qualify as "Eligible Securities." The directors of the funds determined that it would not be in the best interests of the fund to sell the notes and instead obtained an agreement from an affiliate of the adviser to reimburse the fund if the debtor failed to pay the principal or interest due on the notes. These reimbursement obligations were secured by an irrevocable standby letter of credit issued by a bank with a credit rating of sufficient quality to allow the letter of credit to be treated as an "Eligible Security." Because the reimbursement and/or letter of credit arrangement was entered into by an affiliate of the investment adviser, the funds were concerned that such transactions could constitute violations of the restrictions against affiliate transactions contained in Sections 12(d)(3), 17(a) and 17(d) and Rule 17d-1 of the Investment Company Act. The SEC staff stated that it would not recommend enforcement action provided various conditions were met, including the requirement that the letter of credit was issued at no cost to the fund (*i.e.*, the adviser paid the fee). SEI Daily Income Trust-Money Market Fund, SEC Staff No-Action Letter (November 9, 2007), SEI Daily Income Trust-Prime Obligation Fund, SEC Staff No-Action Letter (November 8, 2007) and STI Classic Funds, SEC Staff No-Action Letter (October 26, 2007).

Elizabeth G. Osterman Named Associate Director in the SEC's Division of Investment Management

The Securities and Exchange Commission announced that Elizabeth G. Osterman has been named Associate Director of Exemptive Applications and Special Projects in the agency's Division of Investment Management. Ms. Osterman will oversee the Investment Company Act exemptive applications process and a new office in the Division of Investment Management dedicated to special projects.

Contact Information

For further information, please contact the Ropes & Gray attorney who normally advises you.