

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

## SEC Releases Pre-Publication Copy of RAND Study of Broker-Dealer/Investment Adviser Practices

Recognizing that the constantly evolving market for financial products and services has blurred the dividing line between broker-dealers (“BDs”) and investment advisers (“IAs”), the Securities and Exchange Commission (the “SEC”) retained LRN-RAND Center for Corporate Ethics, Law and Governance (“RAND”) to conduct a study on broker-dealers and investment advisers. A pre-publication copy of this study (the “RAND Study”) was recently made available on the SEC’s website. The RAND Study examines the practices of BDs and IAs in marketing and providing financial products and services to individual investors. The RAND Study also evaluated investors’ understanding of the differences between the BDs’ and IAs’ products, services, duties and obligations. In connection with the first part of its mandate, RAND conducted two sets of interviews: one set with 26 “interested parties” with different perspectives on the industry, and one set with financial services firms. For the second part of the study, RAND sent out survey questionnaires, which were completed by 654 U.S. households, and also conducted interviews with six focus groups consisting of 10-12 individual investors per group.

The results of this research, as reported in the RAND Study, indicate a consensus between both industry participants and investors around the following key points:

- Although the current regulatory scheme treats BDs and IAs differently, in practice their role is viewed as essentially the same by individual investors.
- The primary view of most investors is that, regardless of its regulatory status, the financial intermediary is acting in the investors’ best interests.
- If the services provided by BDs and IAs are functionally the same, the same rules should apply to both types of firms, regardless of the form of compensation they receive for their services.
- Existing disclosures do not provide meaningful help or protection for investors.

It is anticipated that these findings will be an important factor in the SEC’s decision-making on future regulatory developments in this area.

## DOL Proposes ERISA Plan Service Provider Disclosure Regulations

The Department of Labor (“DOL”) recently proposed a regulation regarding new disclosures service providers would be required to provide to ERISA Plan fiduciaries in order for their contract with the plan to fall within the ERISA statutory prohibited transaction exemption for the provision of services. If finalized, compliance with the regulation will effectively be required because the provision of services to an ERISA Plan otherwise would generally be a nonexempt prohibited transaction exposing the service provider to certain liabilities. Generally, the regulation would apply to three categories of service providers: those who provide services to the plan as a fiduciary within the meaning of section 3(21) of ERISA or under the Investment Advisers Act of 1940; those who provide specific services, including banking, consulting, custodial, insurance, investment advisory, investment management, recordkeeping, securities or other brokerage, or other third party administration; and those who receive indirect compensation for accounting, actuarial, appraisal, auditing, legal, or valuation services. Among other requirements under the regulation, service providers would need to disclose the compensation and

fees, and manner in which they will be received, for each service provided to the plan. The service provider must also provide information regarding actual or potential conflicts of interest it might have. Such disclosures concerning conflicts include:

- Whether the provider or an affiliate expects to participate in or to acquire a financial or other interest in any transaction to be entered into in connection with the contract or arrangement, and if so, a description of the transaction and the service provider's interest.
- Whether the service provider or an affiliate has a material relationship with a money manager, broker, client, service provider to the plan, or any other entity that creates or may create a conflict of interest in performing services under the contract or arrangement, and if so, a description of the relationship.
- Whether the service provider or an affiliate will be able to affect its own compensation or fees (for example, as a result of performance-based compensation) without the prior approval of an independent plan fiduciary, and if so, a description of the nature of the compensation.
- An explanation of any policies or procedures the service provider or an affiliate has to address actual or potential conflicts of interest.

Under the DOL's proposed regulations, a plan fiduciary who discovers that a service provider failed to make the necessary disclosures would be required to send to the service provider a written request that the appropriate disclosures be made and provide notice to the DOL if the service provider fails to provide such disclosures within 90 days. The DOL proposes that the new rules be effective 90 days after publication of the final regulation. Comments on the proposed regulation are due by February 11, 2008.

### Delaware Bankruptcy Court Upholds Bankruptcy "Safe Harbor" for Mortgage Loan Repurchase Transactions

In a case of first impression, the United States Bankruptcy Court in Delaware has rejected an attempt by a Chapter 11 debtor to recharacterize a mortgage loan repurchase agreement ("repo") as a secured loan and has upheld Bankruptcy Code provisions that provide a "safe harbor," exempting repo transactions from the automatic stay and other provisions that might impede orderly termination of the repo in the event of bankruptcy of a counterparty. In the case, Calyon New York Branch v. American Home Mortgage Corp., the court noted that, in order to preserve liquidity in repo markets, Congress intended to eliminate any inquiry as to whether a repurchase or reverse repurchase transaction is a purchase and sale transaction or a secured financing. The court applied a mechanical, plain language approach in determining that the mortgage loan repurchase transaction at issue met the requirements for the statutory "safe harbor." In a victory for the debtor, however, the court held that contract provisions related to the debtor's retention of mortgage loan servicing rights were severable from the repo transaction. The court upheld the debtors' right to continue to collect fees for service of the mortgage loans notwithstanding the termination of the repurchase agreement.

### Mutual Fund Permitted to Exclude Proposal of "Nominal Proponent" of Shareholder Activist Investors

In a recent No Action Letter, the SEC staff indicated that it would not recommend enforcement action if an investment company (the "Trust") excluded the shareholder proposal described below from its proxy material. The Trust applied for relief after it received a shareholder proposal submitted by Andrew Dakos on behalf of Full Value Partners, L.P., which would have required the Trust to conduct a self-tender offer for all of the outstanding shares of the Trust at net asset value. The Trust argued that the proposal could be excluded from its proxy material under Rule 14a-8(h) of the Securities and Exchange Act of 1934, which requires a shareholder who has submitted a proposal to appear personally at the share-

holders' meeting or send a representative to present the proposal or provide good cause for failing to appear. The Trust stated that it had included in its proxy materials for a prior shareholder meeting a shareholder proposal submitted by Phillip Goldstein on behalf of Opportunity Partners, L.P. (the "Previous Proposal"). Based on filings with the SEC, the Trust stated that Messrs. Goldstein and Dakos, Opportunity Partners and Full Value Partners were all members of the Bulldog Investors Shareholders group, and that the SEC filings evidenced their practice of voting their shares as a group. The Trust further stated that neither Opportunity Partners nor any other members of Bulldog Investors attended or sent a representative to the shareholder meeting at which the Previous Proposal was scheduled to be discussed, or provided an explanation as to why they failed to do so. The Trust argued that as a result of these facts, it was entitled to exclude any proposals that Full Value Partners, Dakos, Goldstein, Opportunity Partners, Bulldog Investors or other "nominal proponents" of these parties may submit for inclusion in the Trust's 2008 and 2009 proxy materials. In granting the requested no-action relief, the SEC Staff rejected Mr. Dakos' argument that Opportunity Partners is a distinct legal entity from Full Value, and therefore should not be deemed to be a "nominal proponent" of Opportunity Partners. [Franklin Universal Trust](#), SEC No-Action letter dated December 18, 2007.

### Hedge Fund Pays \$1.1 Million Civil Penalty for Hart-Scott-Rodino Filing Violations

On December 19, 2007, the Federal Trade Commission ("FTC") announced the filing and settlement of a federal district court action against ValueAct Capital Partners, L.P. alleging violations related to the acquisitions of stock of three companies for failure to make required filings under the Hart-Scott-Rodino Premerger Notification Act ("HSR Act"). According to the FTC, ValueAct violated the HSR Act's reporting requirements in 2005 when it acquired voting securities of Gartner, Inc., Catalina Marketing Group, and Acxiom Corp. ValueAct had made three similar violations in 2003. In many circumstances, the HSR Act requires a purchaser who meets the thresholds of the Act to file a notification and observe the premerger waiting period before acquiring more than \$59.8 million (the current threshold amount, adjusted annually) of an issuer's voting securities (if no exemption applies). In many circumstances, the purchaser must make another HSR filing and observe the waiting period before acquiring more than \$119.6 million of the voting securities of that entity (if no exemption applies). Among the exemptions under the HSR Act is the "passive investor" exemption, which provides that acquisitions made solely for the purpose of investment are exempt from the reporting requirements if, as a result of the acquisition, the securities held do not exceed 10 percent of the outstanding voting securities of the issuer. The HSR Act imposes penalties for each day that the company holds stock that it acquired without complying with the HSR Act requirements.

### Contact Information

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

