

shareholders (unless the Fund's obligations under the Plan have been assumed by a financially responsible party purchasing such assets) or in the event of a merger or reorganization of a Fund (unless prior to such merger or reorganization, the Fund's board of directors determines that the Plan shall survive the merger or reorganization), all unpaid amounts in the Deferred Fee Accounts maintained by such Fund shall be paid in a lump sum to the Eligible Directors on the effective date thereof.<sup>2</sup> The Plan will not obligate any participating Fund to retain a director in such a capacity, nor will it obligate any Fund to pay any (or any particular level of) directors' fees to any director.

#### Applicants' Legal Analysis

1. Applicants request an order which would exempt the Funds: (a) under section 6(c) of the Act from sections 13(a)(2), 13(a)(3), 18(f)(1), 22(f), and 22(g) and rule 2a-7 thereunder, to the extent necessary to permit the Funds to adopt and implement the Plan; (b) under sections 6(c) and 17(b) of the Act from section 17(a)(1) to permit the Funds to sell securities for which they are the issuer to participating Funds in connection with the Plan; and (c) under section 17(d) of the Act and rule 17d-1 thereunder to permit the Funds to effect certain joint transactions incident to the Plan.

2. Section 18(f)(1) generally prohibits a registered open-end investment company from issuing senior securities. Section 13(a)(2) requires that a registered investment company obtain shareholder authorization before issuing any senior security not contemplated by the recitals of policy in its registration statement. Applicants state that the Plan possesses none of the characteristics of senior securities that led Congress to enact section 18(f)(1). The Plan would not: (a) induce speculative investments or provide opportunities for manipulative allocation of any Fund's expenses or profits; (b) affect control of any Fund; or (c) confuse investors or convey a false impression as to the safety of their investments. All liabilities created under the Plan would be offset by equal amounts of assets that

would not otherwise exist if the fees were paid on a current basis.

3. Section 22(f) prohibits undisclosed restrictions on transferability or negotiability of redeemable securities issued by open-end investment companies. The Plan would set forth all such restrictions, which would be included primarily to benefit the Eligible Directors and would not adversely affect the interests of the directors or of any shareholder.

4. Section 22(g) prohibits registered open-end investment companies from issuing any of their securities for services or for property other than cash or securities. This provision prevents the dilution of equity and voting power that may result when securities are issued for consideration that is not readily valued. Applicants believe that the Plan would merely provide for deferral of payment of such fees and thus should be viewed as being issued not in return for services but in return for a Fund not being required to pay such fees on a current basis.

5. Section 13(a)(3) provides that no registered investment company shall, unless authorized by the vote of a majority of its outstanding voting securities, deviate from any investment policy that is changeable only if authorized by shareholder vote. The relief requested from section 13(a)(3) would extend to Future Funds for which Morgan Stanley becomes investment adviser subsequent to such Future Fund's initial public offering and that have investment policies prohibiting the purchase of investment company shares without shareholder approval. Applicants believe that relief from section 13(a)(3) is appropriate to enable the affected Funds to invest in Underlying Securities without a shareholder vote. Applicants will provide notice to shareholders in the prospectus of each affected Fund of the Deferred Compensation under the Plan. The value of the Underlying Securities will be *de minimis* in relation to the total net assets of the respective Fund, and will at all times equal the value of the Fund's obligations to pay deferred fees (plus any increase in value thereof.)

6. Rule 2a-7 imposes certain restrictions on the investments of "money market funds," as defined under the rule, that would prohibit a Fund that is a money market Fund from investing in the shares of any other Fund. Applicants believe that the requested exemption would permit the Funds to achieve an exact matching of Underlying Securities with the deemed investments of the Deferred Fee Accounts, thereby ensuring that the

deferred fees would not affect net asset value.

7. Section 6(c) provides, in relevant part, that the SEC may, conditionally or unconditionally, by order, exempt any person or class of persons from any provision of the Act or from any rule thereunder, if such exemption is necessary or appropriate in the public interest, consistent with the protection of investors, and consistent with the purposes fairly intended by the policy and provisions of the Act. Applicants submit that the relief requested from the above provisions satisfies this standard.

8. Section 17(a)(1) generally prohibits an affiliated person of a registered investment company from selling any security to such registered investment company. Funds that are advised by the same entity may be "affiliated persons" under section 2(a)(3)(C) of the Act.<sup>3</sup> Applicants assert that section 17(a)(1) was designed to prevent, among other things, sponsors of investment companies from using investment company assets as capital for enterprises with which they were associated or to acquire controlling interest in such enterprises. Applicants submit that the sale of securities issued by the Funds pursuant to the Plan does not implicate the concerns of Congress in enacting this section, but merely would facilitate the matching of each Fund's liability for deferred directors' fees with the Underlying Securities that would determine the amount of such Fund's liability.

9. Section 17(b) authorizes the SEC to exempt a proposed transaction from section 17(a) if evidence establishes that the terms of the transaction, including the consideration to be paid or received, are reasonable and fair and do not involve overreaching on the part of any person concerned, the transaction is consistent with the policies of the registered investment company, and the general purposes of the Act. Applicants assert that the proposed transaction satisfies the criteria of section 17(b). The finding that the terms of the transaction are consistent with the policies of the registered investment company is predicated on the assumption that relief is granted from section 13(a)(3). Applicants also request relief from section 17(a)(1) under section 6(c) to the extent necessary to implement the Deferred Compensation under the Plan on an ongoing basis.

10. Section 17(d) and rule 17d-1 generally prohibit a registered

<sup>2</sup> Applicants acknowledge that the requested order would not permit a party acquiring a Fund's assets to assume a Fund's obligations under the Plan if such obligations would constitute a violation of the Act by the assuming party. Accordingly, such assumption would be permitted only if the assuming party is (a) another Fund, (b) another registered investment company that has received exemptive relief similar to that requested by applicants, or (c) not a registered investment company or is otherwise exempt from the provisions of the Act.

<sup>3</sup> Section 2(a)(3)(C) of the Act defines the term "affiliated person" of another person to include any person directly or indirectly controlling, controlled by, or under common control with such other person.