

proposed external financing limits applicable to the immediate parent of that Financing Entity. However, Applicants request that the underlying intrasystem mirror debt and parent guaranty not be included in that limitation or the separate Scottish Power Guarantee Limitation.

#### X. Proposed Corporate Restructuring

Scottish Power proposes to engage in corporate restructuring or reorganization of the SPUK Group without prior Commission approval.<sup>22</sup> Scottish Power further states that, as it continues to review the combined operations of the Scottish Power System, it may prove prudent to reorganize its nonutility companies to merge current FUCO investments held in the PacifiCorp Group with those of SPUK. Scottish Power also requests authorization to consolidate or otherwise reorganize a nonutility subsidiary if the acquisition of the securities of that nonutility subsidiary is exempt from prior Commission approval. Scottish Power requests that the Commission reserve jurisdiction, pending completion of the record, over any other consolidation or reorganization of its direct or indirect ownership interests in any nonutility company.

#### XI. EWG/FUCO-related Financings

As a general matter, Scottish Power intends to fund its FUCO activities at the level of its first-tier subsidiary, SPUK, or at the level of the Intermediate Companies. However, it may be desirable from time to time for Scottish Power to provide some investment capital or credit support for FUCO acquisitions or operations. To that end, Scottish Power is seeking authority to finance EWG and FUCO investments and operations up to an amount equal to 154% of its consolidated retained earnings ("CRE") at any one time outstanding during the Authorization Period.<sup>23</sup> Applicants state that, as of March 31, 2000, Scottish Power's CRE on a U.S. GAAP basis was \$3,116 million. Applicants further state that, as of March 31, 2000, the Scottish Power System had an existing "aggregate

investment," as that term is defined in rule 53 under the Act, in EWGs and FUCOs of an amount equal to 104% of Scottish Power's CRE, subject to an adjustment based on the sale of PacifiCorp's Australian FUCO assets.<sup>24</sup> Therefore, Scottish Power's request for an additional investment authorization would result in an aggregate investment of approximately 154% of Scottish Power's CRE, or approximately \$4,797 million.

#### XII. Affiliate Transactions

##### A. Existing Intrasystem Arrangements

PacifiCorp has been providing administrative, management, technical, legal and other support services to its subsidiaries for many years.<sup>25</sup> In addition, there have been occasions when subsidiaries of PacifiCorp have provided services to PacifiCorp or to other PacifiCorp Subsidiaries. Accordingly, PacifiCorp now proposes to continue these arrangements, with PacifiCorp providing services to the PacifiCorp Subsidiaries and on occasion the PacifiCorp Subsidiaries providing services to PacifiCorp and other associate companies in the Scottish Power System. All service transactions will be priced at cost in accordance with section 13(b) of the Act and the rules under the Act.<sup>26</sup>

In addition, SPUK, or another member of the SPUK Group, proposes to perform, on a limited basis, services for the PacifiCorp Group. These services may include: (1) Transition plan preparation and implementation; (2) network performance and customer service improvements; and (3) corporate services. These service transactions also will be priced at cost in accordance with section 13(b) of the Act and the rules under the Act.<sup>27</sup> Applicants state that the costs of services provided by SPUK, or a SPUK, Subsidiary, to the PacifiCorp Group will be directly attributed to PacifiCorp. In the alternative, whenever

<sup>24</sup> As of March 31, 2000, the Scottish Power System had an aggregate investment of \$3,239 million in EWGs and FUCOs.

<sup>25</sup> All affiliate transactions among Scottish Power, PacifiCorp, and the PacifiCorp Subsidiaries are subject to review by all of the state utility commissions that regulate PacifiCorp, including the Idaho Public Utilities Commission, the Public Service Commission of Utah, the Washington Utilities and Transportation Commission, the Public Service Commission of Wyoming, the Oregon Public Utility Commission, and the California Public Utilities Commission.

<sup>26</sup> In the event that the market rate for these service transactions is less than the cost of these services, neither PacifiCorp nor the PacifiCorp Subsidiaries will provide these services.

<sup>27</sup> Scottish Power estimates that the total charges by SPUK to PacifiCorp for the provision of anticipated services will be approximately \$12 million annually.

it is possible to do so accurately, these costs will be attributed to a specific PacifiCorp Subsidiary.

Scottish Power further states that a PacifiCorp Group member may provide incidental services to SPUK or a SPUK Subsidiary at other than cost in compliance with rule 90(d)(1) under the Act. The PacifiCorp Subsidiaries also request authority to provide services and sell goods to SPUK and the SPUK Subsidiaries at fair market prices, under certain circumstances, to any nonutility associates company in the Scottish Power System.

For the Commission by the Division of Investment Management, pursuant to delegated authority.

**Margaret H. McFarland,**

*Deputy Secretary.*

[FR Doc. 00-26379 Filed 10-12-00; 8:45 am]

**BILLING CODE 8010-01-M**

#### SECURITIES AND EXCHANGE COMMISSION

[Investment Company Act Release No. 24680; 812-12094]

#### Vanguard Index Funds, et al.; Notice of Application

October 6, 2000.

**AGENCY:** Securities and Exchange Commission ("Commission").

**ACTION:** Notice of an application for an order under section 6(c) of the Investment Company Act of 1940 ("Act") for exemption from sections 2(a)(32), 18(f)(1), 18(i), 22(d), and 24(d) of the Act and rule 22c-1 under the Act, and under sections 6(c) and 17(b) of the Act for exemption from sections 17(a)(1) and (a)(2) of the Act.

*Summary of Application:* Applicants request an order that would permit each of certain registered open-end management investment companies whose portfolios consist of the component securities of certain indices to issue a new class of shares with limited redeemability. The requested order would permit transactions in the shares of the new classes at negotiated prices in the secondary market and would allow dealers to sell the shares to secondary market purchasers unaccompanied by a prospectus, when prospectus delivery is not required by the Securities Act of 1933. The requested order also would permit certain affiliated persons of the investment companies to deposit securities into, and receive securities from, the investment companies in connection with the purchase and redemption of aggregations of shares of the new classes.

<sup>22</sup> Scottish Power has given commitments to regulators in the U.K. regarding the reorganization of SPUK and its subsidiaries, including the incorporation of divisions of SPUK's business.

<sup>23</sup> Applicants state that Scottish Power's status as a foreign company makes it commercially impossible for it to comply fully with some of the technical requirements of rule 53. In particular, since Scottish Power has pre-existing foreign utility operations, Applicants states that it would be unreasonable to require that Scottish Power maintain the books and records of its FUCOs in accordance with U.S. GAAP, although it will provide reconciliation as required in Form 20-F.

*Applicants:* Vanguard Index Funds (“Index Trust”), The Vanguard Group, Inc. (“VGI”), and Vanguard Marketing Corporation (“VMC”).

*Filing Dates:* The application was filed on May 12, 2000 and was amended on July 12, 2000.

*Hearing or Notification of Hearing:* An order granting the requested relief will be issued unless the Commission orders a hearing. Interested persons may request a hearing by writing to the Commission’s Secretary and serving applicants with a copy of the request, personally or by mail. Hearing requests should be received by the Commission by 5:30 p.m. on October 31, 2000 and should be accompanied by proof of service on applicants, in the form of an affidavit or, for lawyers, a certificate of service. Hearing requests should state the nature of the writer’s interest, the reason for the request, and the issues contested. Persons may request notification of a hearing by writing to the Commission’s Secretary.

**ADDRESSES:** Secretary, Securities and Exchange Commission, 450 Fifth Street, NW, Washington, DC 20549-0609. Applicants, P.O. Box 2600, Valley Forge, PA 19482.

**FOR FURTHER INFORMATION CONTACT:** Rachel H. Graham, Senior Counsel, or Michael W. Mundt, Branch Chief, at (202) 942-0564 (Division of Investment Management, Office of Investment Company Regulation).

**SUPPLEMENTARY INFORMATION:** The following is a summary of the application. The complete application may be obtained for a fee at the Commission’s Public Reference Branch, 450 Fifth Street, NW, Washington, DC 20549-0102 (tel. 202-942-8090).

### Applicants’ Representations

1. Index Trust is an open-end management investment company registered under the Act and organized as a Delaware business trust. Index Trust offers nine investment portfolios (each a “Fund” and, collectively, the “Funds”). Currently, eight of the Funds offer separate classes of shares for retail and institutional investors, and the remaining Fund offers retail shares only (shares of the retail and institutional classes of the Funds collectively are referred to as “Conventional Shares”).

2. VGI is a Pennsylvania corporation that is wholly and jointly owned by the Vanguard family of mutual funds (“Vanguard Fund Complex”). VGI is registered as an investment adviser under the Investment Advisers Act of 1940 and as a transfer agent under the Securities Exchange Act of 1934 (“Exchange Act”). VGI provides each

Vanguard fund (including the Funds) with corporate management, administrative, and transfer agency services at cost. VGI also provides advisory services at cost to certain Vanguard funds, including each Fund. VMC is a wholly owned subsidiary of VGI and is registered as a broker-dealer under the Exchange Act. VMC provides all distribution and marketing services at cost to the Vanguard funds including each Fund.

3. Each Fund seeks to track, as closely as possible, the performance of a specified domestic securities index (each an “Index” and, collectively, the “Indices”).<sup>1</sup> A Fund will utilize as an investment approach either a replication strategy or a representative sampling strategy. A Fund using a replication strategy will hold each of the component securities in its Index in about the same proportion as represented in the Index itself. A Fund using a representative sampling strategy will hold a representative sample of the component securities of its Index that resembles the entire Index in terms of industry weightings, market capitalization, price/earnings ratio, dividend yield, and other characteristics. Applicants state that the difference between the performance of a Fund and that of its Index generally has been significantly less than one percentage point. Applicants expect that the Funds will continue to track the Indices with the same degree of precision in the future.

4. Applicants state that some investors trade in and out of the Funds’ Conventional Shares frequently, often as part of a market timing strategy, to the detriment of the Funds’ long-term shareholders. Applicants state that the purchase and redemption requests of market timers increase a Fund’s realization of capital gains, increase Fund expenses, and hinder a Fund’s ability to achieve its investment objective of tracking its Index as closely as possible. According to applicants, Index Trust has adopted policies designed to deter short-term investors, but these efforts have proven insufficient.

5. Each Fund proposes to create a class of shares (Vanguard Index Participation Equity Receipts, or “VIPER

<sup>1</sup> The Indices are the Standard & Poor’s (“S&P”) 500 Composite Stock Price Index, S&P MidCap 400 Index, S&P 500/BARRA Growth Index, S&P 500/BARRA Value Index, S&P Small Cap 600/BARRA Growth Index, S&P Small Cap 600/BARRA Value Index, Wilshire 5000 Total Market Index, Wilshire 4500 Completion Index, and Russell 200 Index. No entity that creates, complies, sponsors, or maintains an Index is an affiliated person, as defined in section 2(a)(3) of the Act, or an affiliated person of an affiliated person, of the Funds, VGI, or VMC.

Shares”) that would be listed on a national securities exchange (“Exchange”) and would trade in the secondary market at negotiated prices. Applicants state that, by creating exchange-traded classes of shares, the Funds hope to provide short-term investors with an attractive means of purchasing Fund shares that can be bought and sold continuously throughout the day at market prices.<sup>2</sup> Applicants further assert that the new classes of VIPER Shares would benefit holders of Conventional Shares by reducing the portfolio disruption and transaction costs caused by market timing activity.

6. Except in connection with the Exchange Option (defined below), the Funds will sell VIPER Shares in aggregations of a specified number ranging from 20,000 to 200,000 shares (“Creation Units”), depending on the Fund. The price of a Creation Unit will range from about \$2,000,000 to \$6,000,000.<sup>3</sup> Creation Units may be purchased only by or through (i) a participant in the Continuous Net Settlement System of the National Securities Clearing Corporation (“NSCC”) or (ii) a Depository Trust Company (“DTC”) participant. In either case, the participant must enter into a participant agreement with VMC. Creation Units will be issued in exchange for an in-kind deposit of securities and cash. An investor wishing to purchase a Creation Unit from a Fund will have to transfer to the Fund a “Portfolio Deposit” consisting of (i) a basket of securities selected by VGI from among the securities contained in the Fund’s portfolio (“Deposit Securities”),<sup>4</sup> and (ii) a cash payment to equalize any difference between (a) the total aggregate market value of the Deposit Securities and (b) the NAV per Creation Unit of the Fund (“Balancing Amount”).<sup>5</sup> An investor purchasing a

<sup>2</sup> Transactions in each Fund’s Conventional Shares would continue to be priced at that day’s net asset value (“NAV”), which is calculated once per day at the close of trading on the New York Stock Exchange.

<sup>3</sup> A Fund may require that an investor purchase a minimum number of Creation Units.

<sup>4</sup> Applicants state that, for Funds holding fewer than approximately one thousand portfolio securities, the Deposit Securities typically will be identical to the Fund’s portfolio. For Funds holding more than that number of portfolio securities, VGI will select a subset of the Fund’s portfolio using a representative sampling strategy.

<sup>5</sup> On each business day, VGI will make available through the NSCC, prior to the opening of trading on the Exchange, the list of the names and the required number of shares of each Deposit Security for each Fund. In addition, each Fund reserves the right to permit or require the substitution of an amount of cash to be added to the Balancing Amount, or of a different security, to replace any Deposit Security in certain circumstances.

Creation Unit from a Fund will be charged a fee ("Transaction Fee") to prevent the dilution of the interests of the remaining shareholders resulting from the Fund incurring costs in connection with the purchase of the Creation Units.<sup>6</sup> Each purchaser of a Creation Unit will receive a prospectus for the VIPER Shares ("VIPER Shares Prospectus") that contains complete disclosure about the Transaction Fee. A Fund's Conventional Shares will be covered by a separate prospectus ("Conventional Shares Prospectus").

7. Orders to purchase Creation Units will be placed with VMC, which will be responsible for transmitting the orders to the applicable Fund. VMC will maintain a record of Creation Unit purchasers and will send out a VIPER Shares Prospectus and confirmation to purchasers whose orders have been accepted by the Fund.

8. Purchasers of Creation Units may separate a Creation Unit into individual VIPER Shares.<sup>7</sup> VIPER Shares will be listed on an Exchange and traded in the secondary market in the same manner as other equity securities. One or more Exchange specialists will be assigned to make a market in VIPER Shares. The price of VIPER Shares traded on an Exchange will be based on a current bid/offer market, and each VIPER Share is expected to have a market value of between \$10 and \$150. Transactions involving the sale of VIPER Shares in the secondary market will be subject to

<sup>6</sup>In situations where a Fund permits a purchaser to substitute cash for one or more Deposit Securities, the purchaser will be assessed a higher Transaction Fee to offset the increased cost to the Fund of buying those particular Deposit Securities.

<sup>7</sup> Applicants state that persons purchasing Creation Units will be cautioned in the VIPER Shares Prospectus that some activities on their part may, depending on the circumstances, result in their being deemed statutory underwriters and subject them to the prospectus delivery and liability provisions of the Securities Act of 1933 ("Securities Act"). For example, a broker-dealer firm may be deemed a statutory underwriter if it purchases Creation Units from a Fund, breaks them down into the constituent VIPER Shares, and sells VIPER Shares directly to its customers; or if it chooses to couple the purchase of a supply of new VIPER Shares with an active selling effort involving solicitation of secondary market demand for VIPER Shares. The VIPER Shares Prospectus will state that whether a person is an underwriter depends upon all the facts and circumstances pertaining to that person's activities. The VIPER Shares Prospectus also will state that broker-dealer firms should note that dealers who are not "underwriters" but are participating in a distribution (as contrasted to ordinary secondary trading transactions), and thus dealing with VIPER Shares that are part of an "unsold allotment" within the meaning of section 4(3)(C) of the Securities Act, would be unable to take advantage of the prospectus delivery exemption provided by section 4(3) of the Securities Act.

customary brokerage commissions and charges.

9. Applicants expect that purchasers of Creation Units will include institutional investors and arbitrageurs. An Exchange specialist, in providing for a fair and orderly secondary market for VIPER Shares, also may purchase Creation Units for use in its market-making activities on the Exchange. Applicants expect that secondary market purchasers of VIPER Shares will include both institutional and retail investors.<sup>8</sup> Applicants believe that arbitrageurs will purchase or redeem Creation Units to take advantage of discrepancies between the VIPER Shares' market price and the VIPER Shares' underlying NAV. Applicants expect that this arbitrage activity will provide a market "discipline" that will result in a close correspondence between the price at which the VIPER Shares trade and their NAV. In other words, applicants do not expect the VIPER Shares to trade at a significant premium or discount to their NAV.<sup>9</sup>

10. Applicants will make available a VIPER Shares product description ("Product Description") for distribution in accordance with an Exchange rule requiring Exchange members and member organizations effecting transactions in a Fund's VIPER Shares to deliver a Product Description to investors purchasing VIPER Shares. Applicants state that any other Exchange that applies for unlisted trading privileges in VIPER Shares will have to adopt a similar rule. The Product Description will provide a plain English overview of a Fund, including its investment objective and investment strategies and the material risks and potential rewards of investing in the Fund. The Product Description also will provide a brief, plain English description of the salient aspects of the Fund's VIPER Shares. The Product Description will advise investors that a VIPER Shares Prospectus and the Fund's Statement of Additional Information ("SAI") may be obtained, without charge, from the investor's broker or from VMC. The Product

<sup>8</sup> VIPER Shares will be registered in book-entry form only. DTC or its nominee will be the registered owner of all outstanding VIPER Shares. Records reflecting the beneficial owners of VIPER Shares will be maintained by DTC or its participants.

<sup>9</sup> Every fifteen seconds throughout the trading day, the Exchange will disseminate (i) via the facilities of the Consolidated Tape Association, the market value of a VIPER Share; and (ii) separately from the consolidated tape, a calculation of the estimated NAV of a VIPER Share, which estimate is expected to be accurate to within a few basis points. Applicants state that an investor comparing the two figures will be able to determine whether, and to what extent, VIPER Shares are selling at a premium or discount to NAV.

Description also will provide a website address (in most cases to a website maintained by the sponsor of the relevant Index) where investors can obtain information about the composition and compilation methodology of the Index. Applicants expect that the number of purchases of VIPER Shares in which an investor will not receive a Product Description will not constitute a significant portion of the market activity in VIPER Shares.

11. Except in connection with the liquidation of a Fund or a Fund's VIPER Share class, VIPER Shares will not be individually redeemable. VIPER Shares will only be redeemable in Creation Unit aggregations through each Fund.<sup>10</sup> To redeem, an investor will have to accumulate enough VIPER Shares to constitute a Creation Unit. An investor redeeming a Creation Unit generally will receive (i) a basket of securities ("Redemption Securities") that in most cases will be the same as the Deposit Securities required of investors purchasing Creation Units on the same day, and (ii) a cash payment that generally will be the same as that day's Balancing Amount. An investor also may receive the cash equivalent of a Redemption Security if the Fund determines that such alternative is warranted, such as a case in which the investor is not permitted to own a particular Redemption Security by regulation or policy. A redeeming investor will pay a Transaction Fee to cover the Fund's transaction costs.

12. A Fund may offer holders of its Conventional Shares (except those holding Conventional Shares through a 401(k) or other participant-directed employer-sponsored retirement plan) the opportunity to exchange some or all of those shares for the Fund's VIPER Shares ("Exchange Option").<sup>11</sup> Applicants state that the Exchange Option would facilitate the movement of investors currently holding Conventional Shares, but desiring intraday trading flexibility, out of the Conventional Shares and into VIPER Shares in an expeditious and tax

<sup>10</sup> Creation Units may be redeemed through either NSCC or DTC. Investors who redeem through DTC will pay a higher Transaction Fee.

<sup>11</sup> The terms of an exchange made pursuant to the Exchange Option will comply with section 11(a) of the Act and rule 11a-3 under the Act. The Exchange Option would offer a "one way" exchange only. Therefore, a holder of a Fund's VIPER Shares who wishes to shift his or her investment to the Fund's Conventional Shares would have to sell the VIPER Shares in the secondary market and use the sale proceeds (less brokerage commissions) to purchase Conventional Shares from the Fund. The sale of the VIPER Shares would be a taxable event.

efficient manner.<sup>12</sup> Around the time that the Fund's VIPER Shares begin trading, VGI will send to existing holders of the Fund's Conventional Shares a notice describing the Exchange Option and explaining the process by which an investor may exchange his or her Conventional Shares for VIPER Shares. The notice will comply with section 10(b) of the Securities Act and rule 482 under the Securities Act, and will highlight the key differences between the Fund's VIPER Shares and Conventional Shares. Comparable information about a Fund's Exchange Option also would be contained in a separate section of the Conventional Shares Prospectus. To effect an exchange through the Exchange Option, the investor must have a brokerage account and must contact his or her broker to initiate the exchange. The investor will receive a VIPER Shares Prospectus in connection with the exchange transaction, as required by the Securities Act. Subsequent to the exchange, the investor would have to contact his or her broker for account information relating to his or her VIPER Share holdings or to sell the VIPER Shares.

#### Applicants' Legal Analysis

1. Applicants request an order under section 6(c) of the Act for exemption from sections 2(a)(32), 18(f)(1), 18(i), 22(d), and 224(d) of the Act and rule 22c-1 under the Act; and under sections 6(c) and 17(b) of the Act for exemption from sections 17(a)(1) and (a)(2) of the Act.

2. Section 6(c) of the Act provides that the Commission may exempt any person, security, or transaction, or any class of persons, securities, or transactions, if and to the extent that such exemption is necessary or appropriate in the public interest and consistent with the protection of investors and the purposes fairly intended by the policy and provisions of the Act.

#### Section 2(a)(32) of the Act

3. Section 2(a)(32) of the Act defines a "redeemable security" as any security, other than short-term paper, under the terms of which the holder, upon its presentation to the issuer, is entitled to

<sup>12</sup> An exchange of Conventional Shares for VIPER Shares of the same Fund generally is not a taxable transaction. Applicants note that because DTC's systems currently are unable to handle fractional shares, exchange requests will be rounded down to the nearest whole VIPER Share. If an investor wishes to exchange all of his or her Conventional Shares for VIPER Shares, however, any fractional VIPER Share that results from the exchange would be liquidated and the cash sent to the investor's broker for the benefit of the investor.

receive approximately his proportionate share of the issuer's current net assets, or the cash equivalent. Applicants request an order under section 6(c) of the Act to permit VIPER Shares to be redeemed in Creation Unit aggregations only. Applicants note that because of the arbitrage possibilities created by the redeemability of Creation Units, it is expected that the market price of a VIPER Share will not vary much from its NAV.

#### Sections 18(f)(1) and 18(i) of the Act

4. Section 18(f)(1) of the Act, in relevant part, prohibits a registered open-end company from issuing any class of "senior security," which is defined in section 18(g) of the Act to include any stock of a class having a priority over any other class as to the distribution of assets or payment of dividends. Section 18(i) of the Act requires that every share of stock issued by a registered management company be voting stock, with the same voting rights as every other outstanding voting stock. Rule 18f-3 under the Act permits an open-end fund to issue multiple classes of shares representing interests in the same portfolio without seeking exemptive relief from sections 18(f)(1) and 18(i), provided that the fund complies with certain requirements. Applicants state that they will comply in all respects with rule 18f-3, except the requirements that (i) other than the differences allowed by the rule, each class must have the same rights and obligations as each other class, and (ii) if a class has a different distribution arrangement, the class must pay all of the expenses of that arrangement. Because they may not rely on rule 18f-3, applicants request an exemption under section 6(c) from sections 18(f)(1) and 18(i).

5. Applicants state that there are three ways in which the Conventional Shares and VIPER Shares of each Fund will have different rights: (i) Conventional Shares will be individually redeemable from the Fund, while VIPER Shares will be redeemable only in Creation Unit aggregations; (ii) VIPER Shares will be traded on an Exchange, while Conventional Shares will not; and (iii) Conventional Shares may be exchanged for VIPER Shares, but VIPER Shares may not be exchanged for Conventional Shares. Applicants assert that these different rights are necessary if their proposal is to have the desired benefits. Applicants note that a Fund's VIPER Shares will be tradable on an Exchange and redeemable only in large aggregations, and that its Conventional Shares will be exchangeable for VIPER Shares, in order to encourage short-term

investors to conduct their trading activities in a vehicle that will not disrupt management of the Fund. Applicants assert that there is no reason to make Conventional Shares tradable and that it would be counterproductive to facilitate the ability of market timers to disrupt a Fund by making VIPER Shares individually redeemable or exchangeable for Conventional Shares.

6. Applicants assert that the different rights do not implicate the concerns underlying section 18 of the Act, including conflicts of interest and investor confusion. With respect to the potential for investor confusion, applicants will take a variety of steps to ensure that investors understand the key differences between a Fund's classes of VIPER Shares and Conventional Shares. Applicants state that the VIPER Shares will not be marketed as a mutual fund investment. Marketing materials may refer to VIPER Shares as an interest in an investment company or fund, but will not make reference to an "open-end fund" or "mutual fund" except to compare or contrast the VIPER Shares with the shares of a conventional open-end management investment company. Any marketing or advertising materials addressed primarily to prospective investors will emphasize that (i) VIPER Shares are not redeemable from a Fund other than in Creation Unit aggregations; (ii) VIPER Shares, other than in Creation Unit aggregations, may be sold only through a broker, and the shareholder may have to pay brokerage commissions in connection with the sale; and (iii) the shareholder may receive less than NAV in connection with the sale of VIPER Shares. The same type of disclosure will be provided in the Conventional Shares Prospectus, VIPER Shares Prospectus, Product Description, SAI, and reports to shareholders. Applicants also note that (i) all references to a Fund's exchange-traded class of shares will use a form of the name "VIPERS" rather than the Fund name; (ii) the cover and summary page of the VIPER Shares Prospectus will state that the VIPER Shares are listed on an Exchange and are not individually redeemable; (iii) VMC will not market Conventional Shares and VIPER Shares in the same advertisement or marketing material; and (iv) applicants will prepare educational materials describing the VIPER Shares.

7. Applicants currently allocate distribution expenses among all funds in the Vanguard Fund Complex according to a cost-sharing formula approved by the Commission in 1981 as part of an order allowing the Vanguard Fund Complex to internalize its

distribution services ("1981 Order").<sup>13</sup> For those funds in the Vanguard Fund Complex offering multiple classes of shares (including eight of the Funds), applicants apply the formula in the 1981 Order by treating each class as a separate fund ("Multi-Class Distribution Formula"). Applicants state that the Multi-Class Distribution Formula currently is applied in a manner that is consistent with rule 18f-3 because each class currently has the same distribution arrangement and, accordingly, the rule does not require that each class pay its actual distribution expenses.

8. Applicants propose to apply the Multi-Class Distribution Formula to each Fund's class of VIPER Shares. Applicants acknowledge that, because VIPER Shares may have a distribution arrangement that differs from that for Conventional Shares, the proposed allocation method may be inconsistent with the rule. Applicants contend, however, that the Multi-Class Distribution Formula is a fundamental feature of Vanguard's unique internally managed structure, and that the proposed allocation method is consistent with the method approved by the Commission in the 1981 Order. Applicants represent that prior to the application of the Multi-Class Distribution Formula to a class of VIPER Shares, the board of trustees of Index Trust ("Board"), including a majority of trustees who are not interested persons of Index Trust, as defined in section 2(a)(19) of the Act, will determine for each Fund that the proposed allocation is in the best interests of each class and of the Fund as a whole. As a condition to the order, the Board would be required to make a similar finding for each Fund on an annual basis.

*Section 22(d) of the Act and Rule 22c-1 Under the Act*

9. Section 22(d) of the Act, among other things, prohibits a dealer from selling a redeemable security that is currently being offered to the public by or through an underwriter, except at a current public offering price described in the prospectus. Rule 22c-1 under the

<sup>13</sup> Investment Company Act Rel. No. 11645 (Feb. 25, 1981) (Opinion of the Commission and Final Order). Under the formula, each fund's contribution is based 50% on the fund's average month-end net assets during the preceding quarter relative to the average month-end net assets of the other Vanguard funds, and 50% on the fund's sales of new shares relative to the sales of new shares of the other Vanguard funds during the preceding 24 months. So that a new fund is not unduly burdened, the formula caps each fund's contribution at 125% of the average expenses of the Vanguard funds collectively, with any amounts above the cap redistributed among the other Vanguard funds. In addition, no fund may pay more than 0.2% of its average month-end net assets for distribution.

Act generally requires that a dealer selling, redeeming, or repurchasing a redeemable security do so only at a price based on its NAV. Applicants state that secondary market trading in VIPER Shares will take place at negotiated prices, not at a current offering price described in the VIPER Shares Prospectus, and not at a price based on NAV. Thus, purchases and sales of VIPER Shares in the secondary market will not comply with section 22(d) and rule 22c-1. Applicants accordingly request an exemption under section 6(c) of the Act from these provisions.

10. Applicants assert that the sale of VIPER Shares at negotiated prices does not present the opportunity for any of the abuses that section 22(d) and rule 22c-1 were designed to prevent. Applicants maintain that while there is little legislative history regarding section 22(d), its provisions, as well as those of rule 22c-1, appear to have been designed to (i) prevent dilution caused by certain riskless-trading schemes by principal underwriters and contract dealers; (ii) prevent unjust discrimination or preferential treatment among buyers resulting from sales at different prices; and (iii) assure an orderly distribution of investment company shares by eliminating price competition from dealers offering shares at less than the published sales price and repurchasing shares at more than the published redemption price. Applicants state that secondary market trading in VIPER Shares would not cause dilution for existing Fund shareholders because such transactions would not directly or indirectly affect the Fund's assets. Applicants further state that secondary market trading in VIPER Shares would not lead to discrimination or preferential treatment among purchases because, to the extent different prices exist during a given trading day or from day to day, these variances will occur as a result of market forces. Finally, applicants contend that the proposed distribution system will be orderly because arbitrage activity will ensure that the difference between the market price of VIPER Shares and their NAV remains narrow.

*Section 24(d) of the Act*

11. Section 24(d) of the Act provides, in relevant part, that the prospectus delivery exemption provided to dealer transactions by section 4(3) of the Securities Act does not apply to any transaction in a redeemable security issued by an open-end investment company. Applicants request an exemption under section 6(c) of the Act from section 24(d) to permit dealers selling VIPER Shares to rely on the

prospectus delivery exemption provided by section 4(3) of the Securities Act.<sup>14</sup>

12. Applicants state that VIPER Shares will be listed on an Exchange and will be traded in a manner similar to other equity securities, including the shares of closed-end investment companies. Applicants note that dealers selling shares of closed-end investment companies in the secondary market generally are not required to deliver a prospectus to the purchaser.

13. Applicants contend that VIPER Shares, as a listed security, merit a reduction in the compliance costs and regulatory burdens resulting from the imposition of prospectus delivery obligations in the secondary market. Because VIPER Shares will be exchange-listed, prospective investors will have access to several types of market information about the VIPER Shares. Applicants state that information regarding market price and volume will be continually available on a real-time basis throughout the day on brokers' computer screens and other electronic services. The previous day's price and volume information also will be published daily in the financial section of newspapers.

14. Investors also will receive a Product Description describing the Fund and its VIPER Shares. Applicants state that, while not intended as a substitute for a prospectus, the Product Description will contain information about VIPER Shares that is tailored to meet the needs of investors purchasing VIPER Shares in the secondary market.

*Sections 17(a)(1) and (a)(2) of the Act*

15. Sections 17(a)(1) and (a)(2) of the Act generally prohibit an affiliated person of a registered investment company, or an affiliated person of such person, from selling any security to or purchasing any security from the company. Section 2(a)(3)(A) of the Act defines "affiliated person" as any person owning five percent or more of an issuer's outstanding voting securities. Applicants state that large institutional investors may be affiliated persons of a Fund under section 2(a)(3)(A) and, because purchases and redemptions of Creation Units would be "in-kind" transactions, those investors would be precluded by sections 17(a)(1) and (a)(2) from purchasing or redeeming Creation Units from the Fund. Applicants accordingly request an exemption under sections 6(c) and 17(b) of the Act to permit these affiliated persons to

<sup>14</sup> Applicants do not seek relief from the prospectus delivery requirement for non-secondary market transactions, including purchases of Creation Units or those involving an underwriter and transactions pursuant to the Exchange Option.

purchase and redeem Creation Units from the Fund.

16. Section 17(b) authorizes the Commission 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, and the proposed transaction is consistent with the policies of the registered investment company and the general provisions of the Act. Applicants contend that no useful purpose would be served by prohibiting persons affiliated with a Fund, as described above, from purchasing or redeeming Creation Units from the Fund. Applicants represent that Fund affiliates making in-kind purchases and redemptions would be treated no differently from non-affiliates making the same types of transactions. Applicants state that all purchases and redemptions of Creation Units would be at the Fund's next calculated NAV. Applicants also state that, in all cases, Deposit Securities and Redemption Securities will be valued in the same manner, using the same standards, as those securities are valued for purposes of calculating the Fund's NAV.

Applicants assert that, for these reasons, the requested relief meets the standards of sections 6(c) and 17(b).

#### Applicants' Conditions

Applicants agree that the order granting the requested relief will be subject to the following conditions:

1. No portfolio of Index Trust other than the Funds will issue a class of VIPER Shares unless applicants have requested and received with respect to such portfolio either exemptive relief from the Commission or a no-action letter from the Division of Investment Management of the Commission.

2. The VIPER Shares Prospectus and the Product Description for each Fund will clearly disclose that, for purposes of the Act, VIPER Shares are issued by the Fund and that the acquisition of VIPER Shares by investment companies is subject to the restrictions of section 12(d)(1) of the Act.

3. As long as a Fund operates in reliance on the requested order, the VIPER Shares will be listed on an Exchange.

4. The VIPER Shares of a Fund will not be advertised or marketed as shares of an open-end investment company or mutual fund. The VIPER Shares Prospectus of each Fund will prominently disclose that VIPER Shares are not individually redeemable and will disclose that holders of VIPER Shares may acquire those shares from

the Fund and tender those shares for redemption to the Fund in Creation Unit aggregations only. Any advertised material that describes the purchase or sale of Creation Units or refers to redeemability will prominently disclose that VIPER Shares are not individually redeemable and that holders of VIPER Shares may acquire those shares from the Fund and tender those shares for redemption to the Fund in Creation Unit aggregations only.

5. Before a Fund may rely on the order, the Commission will have approved, pursuant to rule 19b-4 under the Securities Exchange Act of 1934, an Exchange rule requiring Exchange members and member organizations effecting transactions in VIPER Shares to deliver a Product Description to purchasers of VIPER Shares.

6. On an annual basis, the Board, including a majority of trustees who are not interested persons of Index Trust, must determine, for each Fund, that the allocation of distribution expenses among the classes of Conventional Shares and VIPER Shares in accordance with the Multi-Class Distribution Formula is in the best interests of each class and of the Fund as a whole. Index Trust will preserve for a period of not less than six years from the date of a Board determination, the first two years in an easily accessible place, a record of the determination and the basis and information upon which the determination was made. This record will be subject to examination by the Commission and its staff.

7. For six years following the issuance of a Fund's VIPER Shares, the Fund will (i) record and preserve any investor complaints or reports of confusion concerning the Exchange Option that are communicated to the Fund, VGI, and/or VMC; and (ii) record data tracking the number of investors that, after VIPER Shares are offered, purchase the Fund's Conventional Shares and, within 90 days, exchange those shares for VIPER Shares. The Fund will preserve this information in an easily accessible place, and the information will be subject to examination by the Commission and its staff.

8. Applicant's website, which is and will be publicly accessible at no charge, will contain the following information, on a per VIPER Share Basis, for each Fund: (i) The prior business day's NAV and the closing market price, and a calculation of the premium or discount of the closing market price in relation to the NAV; and (ii) data for a period covering at least the four previous calendar quarters (or the life of a Fund, if shorter) indicating how frequently each Fund's VIPER Shares traded at a

premium or discount to NAV based on daily closing market price, and the magnitude of such premiums and discounts. In addition, the Product Description for each Fund will state that applicants' website has information about the premiums and discounts at which the Fund's VIPER Shares have traded.

9. The VIPER Shares Prospectus and annual report will include, for each Fund: (i) the information listed in condition 8(ii), (a) in the case of the VIPER Shares Prospectus, for the most recently completed calendar year (and the most recently completed quarter or quarters, as applicable), and (b) in the case of the annual report, for no less than the immediately preceding five fiscal years (or the life of the Fund, if shorter); and (ii) the cumulative total return and the average annual total return for one, five, and ten year periods (or the life of the Fund, if shorter) of (a) a VIPER Share based on NAV and market price, and (b) the Fund's Index.

By the Commission.

**Jonathan G. Katz,**

*Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

### Sunshine Act Meeting

#### Agency Meeting

Notice is hereby given, pursuant to the provisions of the Government in the Sunshine Act, Pub. L. 94-409, that the Securities and Exchange Commission will hold the following meeting during the week of October 16, 2000.

A closed meeting will be held on Tuesday, October 17, 2000 at 10:30 a.m.

Commissioners, Counsel to the Commissioners, the Secretary to the Commission, and recording secretaries will attend the closed meeting. Certain staff members who have an interest in the matters may also be present.

The General Counsel of the Commission, or his designee, has certified that, in his opinion, one or more of the exemptions set forth in 5 U.S.C. 552b(c)(4), (8), (9)(A) and (10) and 17 CFR 200.402(a)(4), (8), (9)(A) and (10), permit consideration for the scheduled matters at the closed meeting.

The subject matters of the closed meeting scheduled Tuesday, October 17, 2000 will be:

Institution and settlement of injunctive actions; and