for compensation based upon ''a share of capital gains upon or capital appreciation of the funds or any portion of the funds of the client,'' commonly referred to as a ''performance fee.''

2. Section 205(b)(3) provides, in pertinent part, that the performance fee proscriptions of section 205(a)(1) are not applicable to advisory contracts between an investment adviser and a BDC if, among other things, ''the compensation provided for in such contract does not exceed 20 per centum of the realized capital gains upon the funds of [the BDC] over a specified period or as of definite dates, computed net of all realized capital losses and unrealized capital depreciation.'' Thus, Applicants assert, section 205(b)(3) recognizes the appropriateness of a performance fee as compensation for investment advisers to BDCs in light of the special nature of BDCs.

3. Section 205(b)(3) permits a performance fee with respect to realized gains only and does not contemplate the procedures set forth in the Partnership Agreement whereby unrealized gains or losses are ''deemed'' realized under certain conditions for purposes of the compensation formula.

4. Section 206A of the Advisers Act authorizes the Commission, by order upon application, to exempt any person or transaction from any provision of the Advisers Act ''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 Advisers Act].''

5. Applicants request exemptive relief from section 205(a)(1) to permit the Partnership to make in-kind distributions of shares of common stock that ML Oklahoma holds in one of its two remaining investments. Upon distribution, the Partnership would deem realized any unrealized gains or losses on the securities being distributed. Applicants submit that the performance fee received by the Managing General Partner from the in-kind distribution may be prohibited under section 205(a)(1) of the Advisers Act and it is not included within the exemption from that prohibition provided in section 205(b)(3).

6. Applicants state that the exemption sought is consistent with the standards set out in Advisers Act section 206A. Congress has found it appropriate to permit a performance fee in the case of an investment adviser to a BDC. Applicants argue that to the extent section 205(b)(3) requires a performance fee to be based on realized capital gains, their proposal is consistent with the statutory purpose. Once the in-kind distribution is made, the Managing General Partner will no longer have any control over the investment in the subject securities; investors in ML Oklahoma will have the exclusive ability to liquidate such investments. Furthermore, Applicants state that, under the terms of their proposal, the proper valuation of the securities upon which the performance fee is based would be easily determinable. Applicants request exemptive relief only with respect to in-kind distributions of securities that Applicants represent are traded on the NASDAQ NMS and for which market quotations are readily available.[3] Thus, applicants assert, the issues that would be raised if ML Oklahoma paid a performance fee based on the valuation of securities of private companies are not present.

7. Applicants submit that it is in the best interests of the Partners, particularly the Limited Partners, and in the public interest for ML Oklahoma to have the authority to make in-kind distributions of the subject portfolio securities. First, Applicants represent that the distributed securities will be freely transferable, and the Partners will be able to determine whether to hold or sell them. Applicants assert that as a venture capital fund, ML Oklahoma has no experience or expertise with respect to publicly traded securities, and therefore the Partners do not lose the benefits of expert, professional management by receiving in-kind distributions. Second, Applicants assert that the distributions of portfolio securities will not constitute a taxable event with respect to the Partnership or the Partners, so that Partners will, in determining whether to hold or sell the securities, control the timing of realization of capital gains. Third, to the extent that ML Oklahoma holds a significant percentage of the subject company's shares, Applicants expect that the market could more easily absorb sales by those Partners desiring to sell over a more extended time period than if ML Oklahoma sold its position directly over a shorter period of time. Finally, Applicants assert that in-kind distributions on termination are an efficient way of winding up the Partnership's affairs and avoiding premature dispositions of portfolio investments.

[3] In the Application, Applicants state that the relief they request extends to in-kind distributions of securities only if, at the time of the distribution, the securities continue to be traded on a national securities exchange or the NASDAQ NMS.

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

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 00–28793 Filed 11–8–00; 8:45 am]

BILLING CODE 8010–01–M

SECURITIES AND EXCHANGE COMMISSION

[Release No. IC–24725; File No. 812–12136]

Principal Life Insurance Company, et al., Notice of Application

November 2, 2000.

AGENCY: Securities and Exchange Commission (''SEC'' or ''Commission'').

ACTION: Notice of Application for an order pursuant to Section 6(c) of the Investment Company Act of 1940 (the ''1940 Act'') granting exemptions from the provisions of Sections 2(a)(32), 22(c), and 27(i)(2)(A) of the 1940 Act and Rule 22c–1 thereunder to permit the recapture of credits applied to purchase payments made under certain variable annuity contracts.

Summary of Application: Applicants Principal Life Insurance Company (''Principal Life''), Principal Life Insurance Company Separate Account B (the ''Account''), and Princor Financial Services Corporation (''Princor'') seek an order to permit, under specified circumstances, the recovery of certain credits previously applied to purchase payments made under: (i) Certain deferred variable annuity contracts that Principal Life issues through the Account (the contracts, including certain data pages and endorsements, are collectively referred to herein as the ''Contracts''), and (ii) contracts that Principal Life may issue in the future through the Account, any of its other separate accounts, or any separate accounts that it may establish in the future(''Future Accounts'') which contracts are substantially similar in all material respects to the Contracts (''Future Contracts''). Applicants also request that the order extend to any other National Association of Securities Dealers, Inc. (''NASD'') member broker-dealer controlling, controlled by, or under common control with Principal Life, whether existing or created in the future, that serves as a distributor or principal underwriter of the Contracts or any Future Contracts offered through the Account or any Future Accounts (collectively ''Affiliated Broker-Dealers'').

Applicants: Principal Life, the Account, Princor, and any of Principal Life's Future Accounts established to

support Future Contracts issued by Principal Life (collectively, ''Applicants'').

Filing Date: The Application was filed on June 22, 2000 and amended on October 30, 2000.

Hearing or Notification of Hearing: An order granting the Application will be issued unless the SEC orders a hearing. Interested persons may request a hearing by writing to the SEC's Secretary and serving Applicants with a copy of the request, personally or by mail. Hearing requests should be received by the SEC by 5:30 on November 27, 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 who wish to be notified of a hearing may request notification by writing to the SEC's Secretary.

ADDRESSES: Secretary, SEC, 450 5th Street, NW, Washington, DC 20549. Applicants, c/o J. Sumner Jones, Jones & Blouch, L.L.P., 1025 Thomas Jefferson Street, NW., Washington, DC 20007–0805.

FOR FURTHER INFORMATION CONTACT: Rebecca A. Marquigny, Senior Counsel, or Keith Carpenter, Branch Chief, Office of Insurance Products, Division of Investment Management, at (202) 942–0670.

SUPPLEMENTARY INFORMATION: Following is a summary of the Application; the complete Application is available for a fee from the SEC's Public Reference Branch, 450 Fifth Street, NW., Washington, DC 20549–0102 (telephone (202) 942–8090).

Applicants' Representations

1. Principal Life is a stock life insurance company organized under the laws of Iowa in 1879 as Bankers Life Association. It changed its name to Bankers Life Company in 1911, to Principal Mutual Life Insurance Company in 1986, and then to Principal Life Insurance Company in 1998. The name change to Principal Life Insurance Company was made in connection with the reorganization into a mutual holding company structure in 1998. Principal Life's principal business is offering life insurance and annuity contracts in 50 states and the District of Columbia. Principal Mutual Holding company is the holding company of Principal Life, its affiliates and subsidiaries, collectively known as Principal Financial Group.

2. The Account was established in 1970 by Principal Life as a separate account under Iowa law and is registered with the Commission as a unit investment trust under the Act. The Account funds the benefits available under the Contracts and other variable annuity contracts issued by Principal Life. The offering of the Contracts by Principal Life is registered under the Securities Act of 1933. That portion of the assets of the Account that is equal to the reserves and other contract liabilities with respect to the Account is not chargeable with liabilities arising out of any other business of Principal Life. Any income, gains or losses, realized or unrealized, from assets allocated to the Account are, in accordance with the various contracts, credited to or charged against the Account without regard to other income, gains or losses of Principal Life.

3. Princor is an Iowa corporation controlled by Principal Financial Services, Inc. and is the principal underwriter of the Contracts. Princor is registered as a broker-dealer under the Securities Exchange Act of 1934 and is a member of the NASD. Sales of the Contracts are made by registered representatives of broker-dealers authorized by Princor to sell the Contracts. Such registered representatives are also licensed insurance agents or brokers of Principal Life.

4. The Contracts are flexible purchase payment individual deferred combination fixed and variable annuity contracts. The Contracts may be issued under a qualified contract or as a non-qualified contract.

5. The minimum initial purchase payment for a Contract is $2,500 for non-qualified retirement programs and $1,000 for a qualified Contract. The minimum subsequent purchase payment is $100. Principal Life may limit total Contract purchase payments to $2,000,000.

6. At the time of issuance, a Contract owner may elect to purchase the Purchase Payment Credit Rider. If the Rider is elected, Principal Life will add a 5% payment enhancement or credit to the owner's Contract (the ''Credit'') upon receipt of a purchase payment from the Contract owner during the first contract year. After the first contract year, additional purchase payments will not receive a Credit. Principal Life will fund Credits from its general account assets and will allocate Credits among investment options (excluding certain fixed benefit options used for dollar cost averaging (the DCA Plus accounts)) in the same proportion as the applicable purchase payment.

7. Principal Life will recover any Credit applied if the Contract owner returns the Contract for a refund during the 10-day ''free look'' period. The free look period is the 10-day period (or a longer period in states where required) during which a Contract owner may return a Contract after it has been delivered. Upon such return, the Contract owner generally will receive a full refund of the Contract value, less any Credit, and no withdrawal charge will apply to the refund. The Contract owner will retain any earnings attributable to the Credit allocated to his or her account value or, if there has been a decline in the value of accumulation units for an investment to which a Credit has been allocated, will bear the loss from such decline. The refund amount may thus be more or less than the Contract owner's purchase payment. Where applicable state law requires that the full amount of the purchase payment be refunded, the Contract owner will receive that amount, and Principal Life will retain any earnings, or bear any loss, attributable to the Credit as well as to the purchase payment. The recovery of Credits from the sub-accounts will be effected by canceling accumulation units equal in value to the full amounts to be recovered, the number of such units to be calculated at the accumulation unit value next determined. Amounts recovered will be withdrawn from each investment option in the same proportion that the value of the investment account of each investment option bears to the Contract value.

8. Contract owners may allocate their purchase payments among a fixed account, two different DCA Plus fixed options (which will not be available to Contract owners who elect the Purchase Payment (Credit Rider), and a number of sub-accounts of the Account. Each sub-account invests in shares of a corresponding portfolio of certain underlying investment companies (''Underlying Funds''). Principal Life may, subject to compliance with applicable law, add other sub-accounts, eliminate or combine existing sub-accounts or transfer assets in one sub-account to another sub-account established by Principal Life or an affiliated company.

9. The Contracts provide for the following charges: (i) A withdrawal or contingent deferred sales charge (''CDSC'') as a percentage of amounts withdrawn attributable to purchase payments that have been in the Contract less than seven complete years, with the applicable percentage charge declining from a maximum of 6% in years zero, one and two to 0.0% in year seven and thereafter; (ii) an annual contract fee

that is the lesser of $30 or 2% of the accumulated value (which may be waived under certain circumstances); (iii) a daily mortality and expense risks charge in an amount equal on an annual basis to 1.25% of the value of each variable investment account, deducted from each sub-account; and (iv) any applicable state or local premium taxes up to 3.5%, depending on the Contract owner's state of residence or the state in which the Contract was sold. In addition, the Underlying Funds also impose a management and administrative fee which varies depending upon which Funds are selected.

10. If the Purchase Payment Credit Rider is elected, the Contracts will provide for the following charges: (i) A withdrawal or contingent deferred sales charge (''CDSC'') as a percentage of amounts withdrawn attributable to purchase payments that have been in the Contract less than nine complete years, with the applicable percentage charge declining from a maximum of 8% in years zero, one, two and three to 0.0% in year nine and thereafter; (ii) an annual contract fee that is the lesser of $30 or 2% of the accumulated value (which may be waived under certain circumstances); (iii) a daily mortality and expense risks charge in an amount equal on an annual basis to 1.25% of the value of each variable investment account, deducted from each sub-account; (vi) a Purchase Payment Credit Rider charge payable for the first 8 contract years, in an amount equal on an annual basis to .60% of the value of each variable investment account, deducted from each sub-account; and (v) any applicable state or local premium taxes up to 3.5%, depending on the Contract owner's state of residence or the state in which the Contract was sold. In addition, the Underlying Funds also impose a management and administrative fee which varies depending upon which Funds are selected.

11. Because of the higher charges applicable to a Contract with the Purchase Payment Credit Rider, the prospectus description of the Rider will include a statement to the effect that expenses of a Contract with the Rider may be higher than expenses of a Contract without the Rider and the amount of the Credits may be more than offset by the fees and charges associated with the Credits. The prospectus will also state that there may be circumstances in which a Contract owner may be worse off for having the Rider because of the higher charges.

Applicants' Legal Analysis

1. Section 6(c) of the Act authorizes the Commission to exempt any person, security or transaction, or any class or classes of persons, securities or transactions from the provisions of the Act and the rules promulgated thereunder 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. Applicants request that the Commission, pursuant to Section 6(c) of the Act, grant the exemptions requested below with respect to the Contracts, and any Future Contracts funded by the Account or Future Accounts, that are issued by Principal Life and underwritten or distributed by Princor or Affiliated Broker-Dealers. Applicants undertake that Future Contracts will be substantially similar in all material respects to the Contracts. Applicants believe that the requested exemptions are 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.

2. Applicants seek exemption pursuant to Section 6(c) from Sections 2(a)(32), 22(c), and 27(i)(2)(A) of the Act and Rule 22c–1 thereunder to the extend deemed necessary to permit Principal Life to recover any Credit previously applied to purchase payments under certain Contracts or Future Contracts if a Contract owner returns the Contracts or Future Contracts for a refund during the free look period.

3. Applicants represent that it is not administratively feasible to track asset-based charges against Credits in the Account after the Credits have been applied. Accordingly, the asset-based charges applicable to the Account will be assessed against the entire amounts held in the Account, including Credits, during the free look period. As a result, during such period, the aggregate asset-based charges assessed against a Contract owner's annuity account value will be higher than they would have been if the owner's annuity account value did not include any Credits.

4. Subsection (i) of Section 27 of the Act provides that Section 27 does not apply to any registered separate account funding variable insurance contracts, or to the sponsoring insurance company and principal underwriter of such account, except as provided in paragraph (2) of the subsection. Paragraph (2) provides that it shall be unlawful for such a separate account or sponsoring insurance company to sell a contract funded by the registered separate account unless such contract is a redeemable security. Section 2(a)(32) defines a ''redeemable security'' as any security, other than short-term paper, under the terms of which the holder, upon representation to the issuer, is entitled to receive approximately his or her proportionate share of the issuer's current net asserts, or the cash equivalent thereof.

5. Applicants submit that the recovery of Credits in the circumstances set forth in the Application does not deprive a Contract owner of his or her proportionate share of the issuer's current net assets. A Contract owner's interest in the Credit allocated to his or her annuity account value is not vested until the applicable free look period has expired without return of the Contract. Until the right to recovery has expired and any Credit has vested, Principal Life retains the right and interest therein. Thus, when Principal Life recovers any Credit, it is merely retrieving its own assets. The Contract owner is not deprived of a proportionate share of the Account's assets because the Contract owner's interest in such Credit has not vested. Moreover, Principal Life does not recover any earnings attributable to Credits allocated to a Contract owner's account value prior to exercise of the free look return.

6. Applicants further submit that permitting a Contract owner to retain a Credit upon the exercise of the free look return provisions would be unfair and would deny Principal Life a reasonable measure of protection against anti-selection. The anti-selection risk here is that, rather than spreading purchase payments over a number of years, a Contract owner might seek to manipulate Contracts provisions in a manner that leaves Principal Life little time to recover the cost of the Credits. For example, permitting a Contract owner to retain a Credit upon the exercise of the free look return would encourage the purchase of Contracts for a quick profit upon return rather than with the intention of making a long-term investment. As stated above, the amounts recovered will equal the Credits provided by Principal Life from general account assets, and any gains attributable to such Credits will remain a part of the Contract owner's Contract value. For the foregoing reasons, Applicants submit that the provisions for recovery of Credits under the Contracts do not violate Section 2(a)(32) and 27(i)(2)(A) of the Act.

7. Applicants believe, moreover, that the exemptive relief requested is consistent with and serves the stated

purpose of the National Securities Markets Improvement Act of 1996 (''NSMIA'') in amending the Act to ''provide more effective and less burdensome regulation.'' Sections 26(e) and 27(i) were added to the Act to implement the purposes of NSMIA and Congressional intent. The application of Credits to purchase payments under the Contracts should not raise any questions as to Principal Life's compliance with the provisions of Section 27(i). However, to avoid any uncertainty as to full compliance with the Act, Applicants request an exemption from Sections 2(a)(32) and 27(i)(2)(A), to the extent deemed necessary, to permit the recovery of Credits under the circumstances described in the Application with respect to Contracts and Future Contracts, without the loss of relief from Section 27 provided by Section 27(i).

8. Section 22(c) of the Act authorizes the Commission to make rules and regulations applicable to registered investment companies and to principal underwriters of, and dealers in, the redeemable securities of any registered investment company to accomplish the same purposes as contemplated by Section 22(a). Rule 22c–1 thereunder prohibits a registered investment company issuing any redeemable security, a person designated in such issuer's prospectus as authorized to consummate transactions in any such security, and a principal underwriter of, or dealer in, such security, from selling, redeeming, or repurchasing any such security except at a price based on the current net asset value of such security which is next computed after receipt of a tender of such security for redemption or of an order to purchase or sell such security. Principal Life's recovery of Credits as described in the Application might arguably be viewed as involving the redemption of redeemable securities for a price other than one based on the current net asset value of the Account.

9. Applicants believe that the recovery of the Credits does not violate Section 22c–1 and Rule 22c–1. Such recovery does not involve either of the harms that Rule 22c–1 was intended to eliminate or reduce, namely: (i) The dilution of the value of outstanding redeemable securities of registered investment companies through their sale at a price below net asset value or repurchase at a price above it, and (ii) other unfair results, including speculative trading practices. These harms resulted from the practice of basing the price of a mutual fund share on the net asset value per share determined as of the close of the market on the previous day. Such backward pricing allowed investors to take advantage of increases or decreases in net asset value that were not yet reflected in the price, thereby diluting the value of outstanding fund shares.

10. Applicants submit that the recovery of Credits as described in the Application does not pose such a threat of dilution. In effecting recoveries, Principal Life will redeem interests in a Contract owner's Contract at a price determined on the basis of the current net asset value of the sub-account(s) to which the owner's Contract value is allocated. The amounts recovered will equal the Credits that Principal Life has paid out of general account assets. Except where state law requires that the full amount of the purchase payment be refunded, the Contract owners will be entitled to retain any investment gains attributable to the Credits, and the amounts of such gains will be determined on the basis of the current net asset values of the applicable sub-accounts. Under these circumstances, in Applicants' view, the recovery of the Credits does not involve dilution. Applicants further submit that the second harm that Rule 22c–1 was designed to address, namely speculative trading practices calculated to take advantage of backward pricing, will not occur as a result of the recovery of Credits.

11. Applicants contend that, because neither of the harms that Rule 22c–1 was meant to address are found in the recovery of Credits, Rule 22c–1 and Section 22(c) should not be construed as applicable thereto. However, to avoid any uncertainty in this regard, Applicants request an exemption from the provisions of Section 22(c) and Rule 22c–1 to the extent deemed necessary to permit them to recover Credits under the Contracts and Future Contracts as described in the Application.

12. Applicants submit that their request for an order that applies to Future Accounts and Future Contracts that are substantially similar in all material respects to the Contracts and underwritten or distributed by Princor or Affiliated Broker-Dealers is appropriate in the public interest. Such an order would promote competitiveness in the variable annuity market by eliminating the need to file redundant exemptive applications, thereby reducing administrative expenses and maximizing the efficient use of Applicants' resources. Investors will not receive any benefit or additional protection if Applicants are required repeatedly to seek exemptive relief presenting no issue under the Act that has not already been addressed in the Application. Having Applicants file additional applications would impair Applicants' ability to effectively take advantage of business opportunities as they arise. Applicants undertake that Future Contracts funded by the Account or by Future Accounts which seek to rely on the order issued pursuant to this Application will be substantially similar in all material respects to the Contracts.

Conclusion

Section 6(c) of the Act, in pertinent part, provides that the Commission, by order upon application, may conditionally or unconditionally exempt any persons, security or transaction, or any class or classes of persons, securities or transactions, from any provision or provisions of the Act, or any rule or regulation thereunder, 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. Applicants submit that, for the reasons stated in the Application, their exemptive requests meet the standards set out in Section 6(c) and that an order should, therefore, be granted.

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

Jonathan G. Katz,

Secretary.

[FR Doc. 00–28750 Filed 11–8–00; 8:45 am]

BILLING CODE 8010–01–M

SECURITIES AND EXCHANGE COMMISSION

[Investment Company Act Release No. 24727; 812–12244]

Firstar Funds, Inc., et al.; Notice of Application

November 3, 2000.

AGENCY: Securities and Exchange Commission (''Commission'').

ACTION: Notice of an application under section 17(b) of the Investment Company Act of 1940 (the ''Act'') for an exemption from section 17(a) of the Act.

Summary of the Application: Applicants request an order to permit certain series of Firstar Funds, Inc. (''Firstar'') to acquire all of the assets and liabilities of all of the series of Firstar Stellar Funds (''Stellar''), Mercantile Mutual Funds, Inc. (''Mercantile''), and Firstar Select Funds (''Select'') (the ''Reorganizations''). Because of certain affiliations, applicants may not rely on rule 17a–8 under the Act.