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Certification of Management Investment Company Shareholder Reports and Designation of Certified Shareholder Reports as Exchange Act Periodic Reporting Forms; Disclosure Required by Sections 406 and 407 of the Sarbanes-Oxley Act of 2002; Final Rule

SECURITIES AND EXCHANGE COMMISSION

17 CFR Parts 240, 249, 270 and 274

[Release Nos. 34–47262; IC–25914; File Nos. S7–33–02; S7–40–02]

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Certification of Management Investment Company Shareholder Reports and Designation of Certified Shareholder Reports as Exchange Act Periodic Reporting Forms; Disclosure Required by Sections 406 and 407 of the Sarbanes-Oxley Act of 2002

AGENCY: Securities and Exchange Commission.

ACTION: Final rule.

SUMMARY: The Securities and Exchange Commission is adopting rule and form amendments that require registered management investment companies to file certified shareholder reports on Form N–CSR with the Commission, and designating these certified reports as reports that are required under Sections 13(a) and 15(d) of the Securities Exchange Act of 1934 and Section 30 of the Investment Company Act of 1940. The amendments require each registered management investment company's principal executive and financial officers to certify the information contained in these reports in the manner specified by Section 302 of the Sarbanes-Oxley Act of 2002. We are providing that, for registered management investment companies other than small business investment companies, Form N–SAR will be filed under the Investment Company Act of 1940 only and not the Securities Exchange Act of 1934. We are also removing the requirement that Form N–SAR be certified by a registered investment company's principal executive and financial officers. We are also adopting a new rule to require registered management investment companies to maintain disclosure controls and procedures designed to ensure that the information required in reports on Form N–CSR is recorded, processed, summarized, and reported on a timely basis.

In addition, we are adopting forms and amendments that require registered management investment companies to include new disclosures on Form N–CSR or Form N–SAR in order to implement the requirements of Sections 406 and 407 of the Sarbanes-Oxley Act of 2002. First, the rules require a registered management investment company to disclose whether it has adopted a code of ethics that applies to the company's principal executive officer and senior financial officers. An investment company disclosing that it has not adopted such a code must disclose this fact and explain why it has not done so. An investment company also will be required to disclose amendments to, and waivers from, the code of ethics relating to any of those officers. Second, the rules require a registered management investment company to disclose whether it has at least one ''audit committee financial expert'' serving on its audit committee, and if so, the name of the expert and whether the expert is independent of management. An investment company that does not have an audit committee financial expert must disclose this fact and explain why it has no such expert.

DATES: *Effective Date:* March 1, 2003, except that the effective date of the removal of the certification requirement from Form N–SAR for registered management investment companies other than small business investment companies is May 1, 2003.

Compliance Date: See Section III of this release for information on Transition Provisions and Compliance Dates.

FOR FURTHER INFORMATION CONTACT: John M. Faust, Attorney, Katy Mobedshahi, Senior Counsel, Tara L. Royal, Attorney, or Paul G. Cellupica, Assistant Director, Office of Disclosure Regulation, Division of Investment Management, (202) 942–0721, at the Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549–0506.

SUPPLEMENTARY INFORMATION: The Securities and Exchange Commission (''Commission'') is adopting new rules 30a–3 [17 CFR 270.30a–3] and 30d–1 [17 CFR 270.30d–1] under the Investment Company Act of 1940 [15 U.S.C. 80a–1 *et seq.*] (''Investment Company Act''); amendments to rules 8b–15 [17 CFR 270.8b–15], 30a–1 [17 CFR 270.30a–1], 30a–2 [17 CFR 270.30a–2], 30b1–1 [17 CFR 270.30b1–1], 30b1–3 [17 CFR 270.30b1–3], and 30b2–1 [17 CFR 270.30b2–1] under the Investment Company Act; and amendments to rules 12b–25 [17 CFR 240.12b–25], 13a–15 [17 CFR 240.13a–15], and 15d–15 [17 CFR 240.15d–15], and Form 12b–25 [17 CFR 249.322] under the Securities Exchange Act of 1934 [15 U.S.C. 78a *et seq.*] (''Exchange Act''). The Commission also is adopting amendments to Form N–SAR [17 CFR 249.330; 17 CFR 274.101] under the Exchange Act and the Investment Company Act. Finally, the Commission is adopting new Form N–CSR [17 CFR 249.331; 17 CFR 274.128] under the Exchange Act and the Investment Company Act.

I. Introduction and Background

On July 30, 2002, the Sarbanes-Oxley Act of 2002 (''Sarbanes-Oxley Act'') was enacted.[1] Section 302 of the Sarbanes-Oxley Act, entitled ''Corporate Responsibility for Financial Reports,'' required the Commission to adopt final rules to be effective by August 29, 2002, 30 days after the date of enactment, under which the principal executive officer or officers and the principal financial officer or officers, or persons performing similar functions, of an issuer each must certify the information contained in the issuer's quarterly and annual reports filed or submitted under Section 13(a) or 15(d) of the Exchange Act.[2] Form N–SAR currently is the form designated for registered investment companies to comply with their reporting requirements under Sections 13(a) and 15(d) of the Exchange Act, as well as periodic reporting requirements under Sections 30(a) and 30(b)(1) of the Investment Company Act.[3]

On August 28, 2002, the Commission implemented the certification requirement of Section 302 of the Sarbanes-Oxley Act with respect to registered investment companies by adopting new rule 30a–2 under the Investment Company Act and the Sarbanes-Oxley Act.[4] Rule 30a–2 requires a registered investment company that files periodic reports under Section 13(a) or 15(d) of the Exchange Act, *i.e.*, Form N–SAR, to

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[1]

[2] Section 13(a) of the Exchange Act requires every issuer of a security registered pursuant to Section 12 of the Exchange Act to file with the Commission such annual reports and such quarterly reports as the Commission may prescribe. 15 U.S.C. 78m(a). Section 15(d) of the Exchange Act requires each issuer that has filed a registration statement that has become effective pursuant to the Securities Act of 1933 (''Securities Act'') to file such supplementary and periodic information, documents, and reports as may be required pursuant to Section 13 of the Exchange Act in respect of a security registered pursuant to Section 12. 15 U.S.C. 78o(d). The duty of an issuer to file under Section 15(d) is automatically suspended for any fiscal year, other than a fiscal year in which its registration statement becomes effective, if an issuer's securities are held of record by less than 300 persons. 15 U.S.C. 78o(d).

[3] General Instruction A to current Form N–SAR; current Rule 30a–1 under the Investment Company Act [17 CFR 270.30a–1]. See Investment Company Act Release No. 14299 (Jan. 4, 1985) [50 FR 1442 (Jan. 11, 1985)] (release adopting Form N–SAR). Face-amount certificate companies do not file reports on Form N–SAR, but rather file periodic reports on Forms 10–K and 10–Q. See Investment Company Act Release No. 14080 (Aug. 6, 1984) [49 FR 32370, 32372 (Aug. 14, 1984)] (face-amount certificate companies are required to file reports on other forms prescribed under the Exchange Act rather than Form N–SAR).

[4] Investment Company Act Release No. 25722 (Aug. 28, 2002) [67 FR 57276 (Sept. 9, 2002)].

include the certification specified by Section 302 in those periodic reports.

In a companion release, we also proposed to require registered management investment companies to file certified shareholder reports with the Commission on new Form N–CSR and to designate these certified shareholder reports as reports that are required under Sections 13(a) and 15(d) of the Exchange Act and Section 30 of the Investment Company Act.[5] As we noted in that release, we believe that the certification requirement of Section 302 of the Sarbanes-Oxley Act was intended to improve the quality of the disclosure that a company provides regarding its financial condition in its reports to investors.[6] For registered management investment companies, the required reports to shareholders, rather than reports on Form N–SAR, are the primary vehicle for providing financial information to investors. We believe that the information in these reports to shareholders should be certified, and today we are adopting amendments to our forms and rules to require this certification.

In October 2002, we proposed amendments to proposed Form N–CSR and Form N–SAR to implement Sections 406 and 407 of the Sarbanes-Oxley Act with respect to registered investment companies, similar to disclosure requirements that we proposed at the same time with respect to operating companies.[7] Section 406 directs the Commission to adopt rules requiring an issuer to disclose whether or not it has adopted a code of ethics for the issuer's senior financial officers, as well as any change to, or waiver of, that code of ethics. Section 407 directs the Commission to adopt rules: (1) Requiring an issuer to disclose whether or not its audit committee includes at least one member who is a financial expert; and (2) defining the term ''financial expert.'' Earlier this month, we adopted disclosure requirements to implement these provisions with respect to operating companies.[8] Today, we adopt similar disclosure requirements for registered management investment companies.

In the same release in which we proposed to implement Sections 406 and 407, we also proposed amendments to implement Section 404 of the Sarbanes-Oxley Act, relating to internal control reports, with respect to operating companies, as well as certain technical amendments to our rules and forms implementing Section 302 of the Sarbanes-Oxley Act for registered investment companies.[9] We have deferred adoption of the final rules to implement Section 404 to a separate release to be issued at a later date,[10] and we will also consider the technical amendments to our rules and forms implementing Section 302 for registered investment companies at that time.

II. Discussion

The Commission today is adopting new rules, rule and form amendments, and new Form N–CSR under the Investment Company Act to better implement the certification requirement of Section 302 of the Sarbanes-Oxley Act for registered management investment companies, with modifications to address commenters' concerns.[11] Our amendments will require a registered management investment company to file semi-annual reports on Form N–CSR, and will require the certification specified by Section 302 of the Sarbanes-Oxley Act in these semi-annual reports. Further, our amendments will remove the certification requirement from Form N–SAR, with respect to all registered investment companies.[12] In addition, we are adopting rules to require registered management investment companies to maintain, and regularly evaluate the effectiveness of, controls and procedures designed to ensure that the information required in reports on Form N–CSR is recorded, processed, summarized, and reported on a timely basis. Finally, we are adopting amendments to Form N–CSR and Form N–SAR to implement Sections 406 and 407 of the Sarbanes-Oxley Act with respect to registered management investment companies, similar to amendments that we adopted earlier this month to implement these provisions with respect to operating companies.

A. Section 302 of the Sarbanes-Oxley Act—Certification Requirements

1. Certified Shareholder Reports

We are adopting, as proposed, an amendment to rule 30b2–1 under the Investment Company Act, which currently requires registered investment companies to file copies of reports transmitted to shareholders with the Commission within 10 days of their transmission to shareholders. The amendment will require a registered management investment company to file a report with the Commission on new Form N–CSR (''certified shareholder report'') containing (i) a copy of any required shareholder report, (ii) additional information regarding disclosure controls and procedures, and (iii) the certification required by the Sarbanes-Oxley Act.[13] As adopted, new

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[5] *See* Investment Company Act Release No. 25723 (Aug. 30, 2002) [67 FR 57298 (Sept. 9, 2002)] (''Form N–CSR Proposing Release''). The Commission proposed amendments to Form N–CSR in Investment Company Act Release No. 25739 (Sept. 20, 2002) [67 FR 60828 (Sept. 26, 2002)] (proxy voting disclosure); Investment Company Act Release No. 25775 (Oct. 22, 2002) [67 FR 66208 (Oct. 30, 2002)] (code of ethics and financial expert disclosure) (''Section 406/407 Proposing Release''); Investment Company Act Release No. 25838 (Dec. 2, 2002) [67 FR 76780 (Dec. 13, 2002)] (auditor independence provisions of the Sarbanes-Oxley Act); Investment Company Act Release No. 25845 (Dec. 10, 2002) [67 FR 77593 (Dec. 18, 2002)] (revisions to rule 10b–18 under the Exchange Act); Investment Company Act Release No. 25870 (Dec. 18, 2002) [68 FR 160 (Jan. 2, 2003)] (shareholder reports and quarterly portfolio disclosure); and Investment Company Act Release No. 25885 (Jan. 8, 2003) [68 FR 2637 (Jan. 17, 2003)] (standards relating to listed company audit committees).

A management investment company is an investment company other than a unit investment trust or face-amount certificate company. *See* Section 4 of the Investment Company Act [15 U.S.C. 80a–4]. Management investment companies typically issue shares representing an undivided proportionate interest in a changing pool of securities, and include open-end and closed-end companies. *See* T. Lemke, G. Lins, A. Smith III, Regulation of Investment Companies, Vol. I, ch. 4, § 4.04, at 4–5 (2002).

[6] Form N–CSR Proposing Release, *supra* note , 67 FR at 57299.

[7] Section 406/407 Proposing Release, *supra* note 5, 67 FR at 66213–14 and 66217–18.

[8] Securities Act Release No. 8177 (January 23, 2003) (''Section 406/407 Adopting Release'').

[9] Section 406/407 Proposing Release, *supra* note 5, 67 FR at 66222–23.

[10] Section 406/407 Adopting Release, *supra* note 8.

[11] We received 18 comment letters on the Form N–CSR Proposing Release from 17 commenters. The commenters included ten mutual funds, investment advisers, and financial advisers; one trade association; five law firms, law professors, attorneys, and bar associations; and one domestic government agency. These comment letters and a summary of the comments are available for public inspection and copying in our Public Reference Room, 450 Fifth Street, NW., Washington, DC 20549, in File No. S7–33–02. Public comments submitted electronically and a summary of the comments are available on our Web site <*http://www.sec.gov*>.

We received over 200 comment letters on the Section 406/407 Proposing Release, including 23 comment letters on the proposed amendments applicable to investment companies. The commenters included 12 mutual funds and investment advisers; one trade association; four law firms, bar associations, and accounting firms; and six independent directors of investment companies. These comment letters are available for public inspection and copying in our Public Reference Room, 450 Fifth Street, NW., Washington, DC 20549, in File No. S7–40–02. Public comments submitted electronically are available on our Web site <*http://www.sec.gov*>.

[12] Amendments to Item 133 and instructions to Items 77Q3, 102P3, and 133 of Form N–SAR.

[13] Rule 30b2–1(a) under the Investment Company Act [17 CFR 270.30b2–1(a)]; 17 CFR 249.331; 17 CFR 274.128; Items 1, 9, and 10(b) of Form N–CSR. In addition, we are amending rule 30a–2 under the Investment Company Act [17 CFR 270.30a–2] to require Form N–CSR to include the certification required by Section 302 of the Sarbanes-Oxley Act. No certified shareholder report on Form N–CSR

Continued

Form N–CSR requires certified shareholder reports to contain the exact form of the certification prescribed by the form. The certification is required of each principal executive officer and financial officer, and the form of this certification parallels the form of the certification we have prescribed for other Exchange Act reporting forms, such as Forms 10–K and 10–Q. The certification must be filed as an exhibit to a report on Form N–CSR.[14] In addition to the signature required on the certification, the report must be signed by the registrant, and on behalf of the registrant by its principal executive officer or officers and its principal financial officer or officers.[15] The certification requirement will also apply to amendments of certified shareholder reports on Form N–CSR.[16] In addition, we are adopting new rule 30d–1 under the Investment Company Act, designating reports on Form N–CSR as periodic reports filed with the Commission under Section 13(a) or 15(d) of the Exchange Act.[17]

The requirement to file certified shareholder reports will apply to registered management investment companies, regardless of whether they are subject to Section 13(a) or 15(d) of the Exchange Act.[18] By its terms, Section 302 of the Sarbanes-Oxley Act directs the Commission to adopt rules that will apply to companies filing periodic reports under Section 13(a) or 15(d) of the Exchange Act.[19] We believe, however, that it is important for the certification requirement, like our other reporting rules, to apply consistently to all registered investment companies, regardless of whether they fall within the periodic reporting requirements of the Exchange Act.[20]

In light of the adoption of Form N–CSR as an Exchange Act reporting form, we are amending our rules and forms to provide that, for registered management investment companies, Form N–SAR will be filed under the Investment Company Act only and not the Exchange Act.[21] We were persuaded by commenters who argued that certification of both Form N–SAR and shareholder reports would impose an unjustified burden on management investment companies. These commenters noted that Form N–SAR does not contain financial statements; that although Form N–SAR is publicly available, it was developed primarily to elicit information for use by the Commission in its compliance and inspections program; and that the information in Form N–SAR is not generally relied upon by investors.[22] In light of the fact that registered management investment companies will be filing Form N–CSR under the Exchange Act, we do not believe that it is necessary for these companies to continue to file Form N–SAR under the Exchange Act or to certify Form N–SAR under the Sarbanes-Oxley Act.[23] We believe that this is appropriate because, for registered management investment companies, the required reports to shareholders contained in Form N–CSR, rather than Form N–SAR, are the primary vehicle for providing financial statements and other information to investors.[24] The certification requirement was intended to improve the quality of the disclosure that a company provides about its financial condition in its periodic reports to investors.[25]

2. Scope of Certification Requirement

We are adopting, as proposed, the requirement that all of the information filed on Form N–CSR, including all of the information in a shareholder report filed as part of Form N–CSR, be certified. This would include information that is included voluntarily, as well as that required by Form N–CSR. In addition to financial statements, annual reports to shareholders of open-end management investment companies, or mutual funds, typically contain Management's Discussion of Fund Performance (''MDFP''), although, at present, they are not required to do so.[26] MDFP includes narrative disclosure of the factors that materially affected a fund's performance during the reporting period, a line graph comparing the fund's performance to that of an appropriate broad-based market index, and a table of average annual total returns for the fund. In addition, the annual report to shareholders of a management investment company must contain other information, including certain basic information about the investment company's directors.[27]

would be required with respect to a report to shareholders that is not required under rule 30e–1 under the Investment Company Act [17 CFR 270.30e–1], *e.g.*, voluntary quarterly reports. These reports to shareholders would continue to be filed with the Commission as they are presently. Rule 30b2–1(b) under the Investment Company Act [17 CFR 270.30b2–1(b)].

[14] *See* Item 10(b) of Form N–CSR. The EDGAR document type must be EX–99.CERT for an exhibit filed in response to Item 10(b). All certifications in a filing on Form N–CSR should be included in a single EDGAR exhibit document.

[15] *See* General Instruction E to Form N–CSR.

[16] Rule 8b–15 under the Investment Company Act [17 CFR 270.8b–15].

[17] We are also adopting a technical conforming amendment that would delete the language in current rule 30a–1 [17 CFR 270.30a–1] stating that a registered management investment company required to file an annual report pursuant to Section 13(a) or 15(d) of the Exchange Act and Section 30(a) of the Investment Company Act shall be deemed to have satisfied its requirement to file an annual report by the filing of semi-annual reports on Form N–SAR. The amendments rename rule 30a–1 in order to specify that it relates to annual reports by registered unit investment trusts, and rename rule 30b1–1 [17 CFR 270.30b1–1] in order to specify that it relates to semi-annual reports of registered management investment companies.

[18] Rule 30b2–1(a) [17 CFR 270.30b2–1(a)].

[19] *See supra* note (description of Exchange Act reporting requirements).

[20] *Cf.* General Instruction A to Form N–SAR (Form N–SAR is to be used for semi-annual and annual reports by all registered investment companies that have filed a registration statement that has become effective pursuant to the Securities Act, with the exception of face amount certificate companies.).

[21] *See* Rule 30b1–1 under the Investment Company Act [17 CFR 270.30b1–1]; 17 CFR 249.330; 17 CFR 274.101; General Instruction A to Form N–SAR.

[22] *See* Investment Company Act Release No. 14299 (Jan. 4, 1985) [50 FR 1442 (Jan. 11, 1985)] (release adopting Form N–SAR); Investment Company Act Release No. 14080 (Aug. 6, 1984) [49 FR 32370 (Aug. 14, 1984)] (release proposing Form N–SAR).

[23] Instructions to item 77Q3 of Form N–SAR (amended to remove certification); rule 30b1–3 under the Investment Company Act [17 CFR 270.30b1–3] (removing the certification requirement from transition reports on Form N–SAR).

[24] Sections 30(e) and (f) of the Investment Company Act (15 U.S.C. 80a–29(e) and (f)) (requiring a registered investment company to transmit to its stockholders, at least semi-annually, reports containing financial statements and other information prescribed by the Commission).

[25] *See, e.g.*, S. Rep. No. 107–205, at 2 (2002) (''The bill also requires steps to enhance the direct responsibility of senior corporate management for financial reporting and for the quality of financial disclosures made by public companies.''); 148 Cong. Rec. S7355 (July 25, 2002) (statement of Sen. Enzi) (''With respect to section 302, the conference recognizes that results presented in financial statements often necessarily require accompanying disclosures in order to apprise investors of the company's true financial condition and results of operations. The supplemental information contained in these additional disclosures increases transparency for investors. Accordingly, the relevant officers must certify that the financial statements together with the disclosures contained in the periodic report, taken as a whole, are appropriate and fairly represent, in all material respects, the operations and financial condition of the issuer.''); 148 Cong. Rec. S6760 (July 15, 2002) (statement of Sen. Akaka) (''The legislation also requires additional corporate governance procedures to make Chief Executive Officers and Chief Financial Officers more directly responsible for the quality of financial reporting made to investors.'').

[26] Item 5 of Form N–1A. Management's Discussion of Fund Performance must be included in a fund's prospectus unless the fund is a money market fund or the information in the MDFP is included in the fund's annual report to shareholders under rule 30e–1 [17FR 270.30e–1]. A fund that includes MDFP in its annual report must disclose in its prospectus that its annual report contains additional performance information that will be made available upon request and without charge. Item 1(b)(1) of Form N–1A. We recently proposed to require the MDFP to be included in a mutual fund's annual report to shareholders. Investment Company Act Release No. 25870 (Dec. 18, 2002) [68 FR 160, 170 (Jan. 2, 2003)].

[27] Items 13(a)(1) and 22(b)(5) of Form N–1A; Item 18.1 and Instruction 4.e. to Item 23 of Form N–2;

Many commenters objected to our proposal to require certification of all of the information contained in shareholder reports, and instead suggested that the certification should apply only to the financial statements and other financial information in shareholder reports. Commenters argued that the narrative disclosure commonly found in shareholder reports, including the narrative section of MDFP as well as a fund president's letter to shareholders, interviews with portfolio managers, and other similar information that is intended to assist investors in understanding fund performance and portfolio composition, is not analogous to Management's Discussion & Analysis (MD&A) in Form 10–K, and is not the type of objective financial information that the certification requirement of Section 302 was intended to cover.[28] The MD&A, commenters noted, is intended to provide a narrative explanation of an operating company's financial statements and to provide the context within which the financial statements should be analyzed, while the MDFP is simply a narrative explanation of an investment company's performance comparative to the market. These commenters argued that the narrative disclosure in the shareholder reports, including that in the MDFP, does not lend itself to meaningful personal certification by an investment company's principal executive and financial officers, and that requiring certification of the entire shareholder report could have the unintended consequence of encouraging investment companies to reduce the scope of the narrative discussion provided voluntarily in shareholder reports, or even ceasing to provide it altogether.

We are not persuaded by these comments. Section 302 of the Sarbanes-Oxley Act does not limit the scope of the certification to financial information filed by a registrant. The MDFP and other narrative disclosure is relied upon by investors to explain the investment operations and performance of a mutual fund, which is as significant for investors in the fund as management's discussion and analysis of financial condition and results of operations is for investors in an operating company. In its integrated reviews of mutual fund prospectuses and shareholder reports, the staff has identified instances where MDFP has provided insufficient substantive discussion of the factors that affected the fund's performance during the most recent fiscal year. [29] The Commission has asked the staff, in its review of a mutual fund's disclosure documents, to continue to focus on areas where funds' MDFP disclosure has been deficient.[30] We believe that a requirement that MDFP, if included in shareholder reports, must be certified by the mutual fund's principal executive and financial officers, would encourage funds to include a more complete and accurate discussion of the factors that affected fund performance in their MDFP. Further, we note that in the operating company context, reports on Form 10–K contain certain required non-financial information that must be certified.[31]

We also note that the only statement made in the certification with respect to this narrative information is that, based on the certifying officer's knowledge, the report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by the report.[32] This certification is consistent with the current obligation of registrants under the Exchange Act not to file reports that are materially misleading.[33] Therefore, we believe that it is appropriate for the certifying officers to provide assurances to investors that the reports a fund files under the Exchange Act meet this standard.

3. Application of Certification Requirements to Unit Investment Trusts and Small Business Investment Companies

To address commenters' concerns, we are amending Form N–SAR to eliminate the requirement that unit investment trusts (''UITs'') and small business investment companies (''SBICs'') certify their reports on Form N–SAR.[34] Commenters noted that Form N–SAR, which does not contain financial statements, contains little, if any, information regarding a UIT that is of relevance or interest to investors. We agree. Form N–SAR requires both UITs and SBICs to include only limited financial and other information.[35] Because Form N–SAR contains very limited information for UITs and SBICs and is not required to be sent to investors, certification of this information would not promote the intent of Section 302 of the Sarbanes-Oxley Act, which is to improve the quality of the disclosure that a company provides about its financial condition in its periodic reports to investors. We

Item 20(a) and Instruction 4(v) to Item 27(a) of Form N–3.

[28] *See* Item 303 of Regulation S–K [17 CFR 229.303] (Management's Discussion and Analysis).

[29] *See In the Matter of Davis Selected Advisers—NY, Inc.,* Investment Advisers Act Release No. 2055 (Sept. 4, 2002) (fund violated Section 34(b) of the Investment Company Act [15 U.S.C. 80a–34(b)] by failing to disclose the material impact that investments in initial public offerings had on its performance during its previous fiscal year in its MDFP); Tom Lauricella and Aaron Lucchetti, *What's Your Fund Doing? Some Managers Don't Say,* The Wall Street Journal, Oct. 7, 2002, at R23 (describing inadequate discussions in investment companies' MDFP).

[30] Investment Company Act Release No. 25870, *supra* note, 68 FR at 170.

[31] *See* Item 401 of Regulation S–K [17 CFR 229.401] (requiring background information about directors and officers); Section 406/407 Adopting Release, *supra* note (adopting Item 406 of Regulation S–K, which requires disclosure with respect to codes of ethics applicable to a registrant's principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions, and Item 401(h) of Regulation S–K, which requires disclosure of whether a company has at least one audit committee financial expert serving on its audit committee, and if so, the name of the expert and whether the expert is independent of management).

[32] Paragraph 3 of certification exhibit in Item 10(b) of Form N–CSR.

[33] Rule 10b–5 under the Exchange Act [17 CFR 240.10b–5] provides that: ''It shall be unlawful for any person, directly or indirectly, * * * to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading * * *''

[34] Instruction 102P3 of Form N–SAR; Instruction to Item 133 of Form N–SAR.

A UIT is an unmanaged, fixed portfolio of securities that has no corporate management structure, and generally is not required to transmit reports to shareholders containing its financial statements. *See* Section 4(2) of the Investment Company Act [15 U.S.C. 80a–4(2)] (defining UIT). SBICs are management investment companies that are licensed as SBICs under the Small Business Investment Act of 1958. *See* General Instruction A of Form N–5 [17 CFR 239.24; 17 CFR 274.5] (describing SBIC).

[35] UITs report the following information on Form N–SAR: (i) Identifying information (Items 1–6); (ii) the names and addresses of the trust's depositors, sponsors, trustees, principal underwriters, and independent accountants (Items 111–115); (iii) whether the trust is part of a family of investment companies or an insurance company separate account (Items 116–117); (iv) the following numbers: Number of series, dollar amounts of deposits and prior series units, sales charges aggregated for all series, values of and income from various types of securities and expenses aggregated for all series (Items 118–127, 131); (v) information regarding insurance and guarantees (Items 128–130); and (vi) a list of any pre-1972 Investment Company Act file numbers (Item 132). SBICs report the following information on Form N–SAR: (i) Identifying information (Items 1–6); (ii) the names and addresses of the SBIC's advisers, transfer agents, independent accountants, and custodian (Items 89–92); (iii) whether the adviser has clients other than investment companies (Item 93); (iv) whether the SBIC is part of a family of investment companies (Item 94); (v) information on the sales, repurchase and redemptions of the SBIC's securities (Item 95); (vi) securities of the SBIC registered on an exchange (Item 96); (vii) certain financial information, including income, expenses, assets, liabilities, and shareholders' equity (Items 97–101); (viii) exhibits (Item 102); (ix) information on subsidiaries (Items 103–104); and (x) information on fidelity bonds and officers and directors insurance (Items 105–110).

have therefore concluded that requiring UITs and SBICs to certify their reports on Form N–SAR does not produce any meaningful benefit to investors.

While certification of Form N–SAR will no longer be required, UITs and SBICs will continue to file Form N–SAR under both the Exchange Act and the Investment Company Act.[36] UITs and SBICs generally are not required to transmit reports to shareholders containing their financial statements, and UITs and SBICs will not be required to file certified shareholder reports under the Exchange Act.[37] We do not believe that it would be appropriate to remove UITs and SBICs from Exchange Act reporting status by making Form N–SAR an Investment Company Act-only form.

4. Disclosure Controls and Procedures

We are adopting, with modifications to address commenters' concerns, new rule 30a–3, which requires registered management investment companies to maintain, and regularly evaluate the effectiveness of, controls and procedures designed to ensure that the information required in filings on Form N–CSR is recorded, processed, summarized, and reported on a timely basis.[38] Investment companies filing reports under Section 13(a) or 15(d) of the Exchange Act are currently required to maintain disclosure controls and procedures with respect to Exchange Act reports.[39] Rule 30a–3 applies this requirement uniformly to all registered management investment companies, regardless of whether they are subject to Section 13(a) or 15(d) of the Exchange Act.[40] We believe that registered management investment companies filing Form N–CSR should maintain effective disclosure controls and procedures, regardless of whether they fall within the periodic reporting requirements of the Exchange Act. We are also amending the definition of ''disclosure controls and procedures'' in rule 30a–2(c) to make clear that such controls and procedures apply to registered management investment companies regardless of whether they are subject to Section 13(a) or 15(d) of the Exchange Act, and that they do not apply to SBICs and UITs filing Exchange Act reports on Form N–SAR that are not required to be certified.[41]

We are also adopting, as proposed, the requirement of rule 30a–3(b) that a registered management investment company, under the supervision and with the participation of the principal executive and financial officers, conduct an evaluation of its disclosure controls and procedures within the 90-day period prior to the filing date of each Form N–CSR requiring certification under Investment Company Act rule 30a–2.[42] We expect that this evaluation will be carried out in a manner that will form the basis for the certification required by Section 302 of the Sarbanes-Oxley Act regarding disclosure controls and procedures required by Investment Company Act rule 30a–2(b)(4).[43]

As proposed, rule 30a–3 would have extended the requirement to maintain and evaluate disclosure controls and procedures to filings under the Securities Act of 1933 (''Securities Act'') and the Investment Company Act.[44] Commenters argued that this extension would impose a larger burden on investment companies than on operating companies, which are only required to maintain disclosure controls and procedures with respect to their Exchange Act reports. Commenters pointed out that under the rule, as proposed, investment companies would have to establish and maintain, and conduct evaluations of the effectiveness of, disclosure controls and procedures on at least a semi-annual basis, with respect to all of the updates of their registration statements, as well as with respect to other filings required under the Securities Act and the Investment Company Act, including advertisements and sales literature.[45] According to commenters, these periodic evaluations would add substantially to the workload of fund officers, but would not result in a discernible benefit to fund shareholders or further the intent of the Sarbanes-Oxley Act.

Section 302 of the Sarbanes-Oxley Act does not require evaluations of disclosure controls and procedures with respect to non-Exchange Act filings, and we have determined that it would not be appropriate to extend this requirement to Securities Act and Investment Company Act filings at this time. We are concerned that the evaluation process could be unduly burdensome, relative to its benefits, when applied to these other filings. Therefore, we are limiting the requirement to maintain and evaluate disclosure controls and procedures to Form N–CSR, the Exchange Act document that will be subject to the Sarbanes-Oxley Act certification requirements.

We wish to emphasize that effective disclosure controls and procedures are essential for an investment company to meet its disclosure obligations under all of the securities laws, including the Securities Act and the Investment Company Act. Our limitation of the definition of disclosure controls and procedures to Form N–CSR in the rules we adopt today in no way diminishes the importance of disclosure controls and procedures designed to ensure that the information required in other filings made by an investment company, including prospectuses and prospectus amendments, advertisements and sales literature, and Form N–SAR, is recorded, processed, summarized, and reported on a timely basis. Our determination to limit the scope of disclosure controls and procedures in these rules rests on our concern that the burdens of the specific evaluation

[36] Rules 30a–1, 30b1–1, and 30d–1 under the Investment Company Act [17 CFR 270.30a–1; 17 CFR 270.30b1–1; 17 CFR 270.30d–1]; 17 CFR 249.330; 17 CFR 274.101; General Instruction A to Form N–SAR.

[37] Rules 30b2–1(a) and 30d–1 under the Investment Company Act [17 CFR 270.30b2–1(a); 17 CFR 270.30d–1] and General Instruction A to Form N–CSR [17 CFR 249.331; 17 CFR 274.128]. SBICs are not required under rule 30e–1(a) [17 CFR 270.30e–1(a)] to transmit reports to shareholders containing their financial statements, because Form N–5 [17 CFR 239.24; 17 CFR 274.5], the registration form for SBICs, does not prescribe requirements for reports to shareholders by SBICs.

[38] 17 CFR 270.30a–3. SBICs will not be required to maintain disclosure controls and procedures as required by rule 30a-3 because they do not file reports on Form N–CSR. *See supra* note 37.

[39] Rules 13a–15 and 15d–15 under the Exchange Act [17 CFR 240.13a–15; 17 CFR 15d–15].

[40] *See supra* note 2 (description of Exchange Act reporting requirements).

[41] Rule 30a–2(c) under the Investment Company Act [17 CFR 270.30a–2(c)]. We are also adopting conforming amendments to rules 13a–15 and 15d–15 under the Exchange Act [17 CFR 240.13a–15; 17 CFR 240.15d–15] to exclude SBICs and UITs from the requirements to maintain disclosure controls and procedures under those rules.

[42] 17 CFR 270.30a–3(b).

[43] We recognize that, in the case of a series fund or family of investment companies, the disclosure controls and procedures for each fund in the series or family may be the same. Therefore, for purposes of Rule 30a–2(b)(4)(ii) and (iii), a single evaluation of the effectiveness of the disclosure controls and procedures for the series or family could be used in multiple certifications for the funds in the series or family, as long as the evaluation has been performed within 90 days of the date of the report on Form N–CSR.

[44] Form N–CSR Proposing Release, *supra* note, 67 FR at 57306 (proposed rules 30a–2(c) and 30a–3 under the Investment Company Act).

[45] Section 24(b) of the Investment Company Act [15 U.S.C. 80a–24(b)] requires investment companies to file ''any advertisement, pamphlet, circular, form letter, or other sales literature'' with the Commission. Rule 24b–3 under the Investment Company Act [17 CFR 270.24b–3] permits investment companies to satisfy this requirement by filing sales literature with the National Association of Securities Dealers, Inc. (''NASD'') or another national securities association registered under Section 15A of the Exchange Act [15 U.S.C. 78o]. Rule 497(a)(1) under the Securities Act [17 CFR 230.497(a)(1)] requires an investment company advertisement pursuant to rule 482 under the Securities Act [17 CFR 230.482] to be filed with the Commission, and rule 497(i) under the Securities Act [17 CFR 230.497(i)] permits a rule 482 advertisement to be considered filed with the Commission if it is filed with the NASD or another national securities association registered under Section 15A of the Exchange Act.

process mandated by the rules may outweigh its benefits when extended to these other filings.

5. Extension of Time for Filing Form N–CSR

We are also adopting amendments to require an investment company to file a Form 12b–25 if it will not be able to file a report on Form N–CSR in a timely manner.[46] Filing of a Form 12b–25 would provide the investment company with an automatic extension of time to file Form N–CSR of up to 15 calendar days following the prescribed due date. Form 12b–25 currently may be used for reports on Form N–SAR, and we note that the form will continue to be available to all filers on Form N–SAR, including registered management investment companies filing exclusively under the Investment Company Act.

B. Section 406 of the Sarbanes-Oxley Act—Code of Ethics

We are adopting, with modifications to address commenters' concerns, our proposed amendments that implement Section 406 of the Sarbanes-Oxley Act with respect to registered management investment companies. These requirements are similar to those we recently adopted for operating companies, and we direct investment companies to that release for information concerning these requirements.[47] The amendments we are adopting will require a registered management investment company to:

- Disclose annually whether the investment company has adopted a code of ethics that applies to the investment company's principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions, regardless of whether these individuals are employed by the investment company or a third party;[48]
- If the investment company has not adopted a code of ethics, explain why it has not done so;[49]
- Describe briefly the nature of any amendment to, or waiver from a provision of, the investment company's code of ethics in its report on Form N–CSR or Form N–SAR, as applicable. In the alternative, the investment company may disclose this information on its Internet website within five business days following the date of the amendment or waiver, if the investment company has disclosed in its most recently filed report on Form N–CSR or Form N–SAR its intention to provide disclosure in this manner and its Internet address, it makes the information available on its website for a 12-month period, and it retains the information for a period of not less than six years following the end of the fiscal year in which the amendment or waiver occurred.[50]

The rules, as adopted, reflect modifications that are similar to those we recently made to the proposed code of ethics disclosure requirements for operating companies, for the reasons described in the release adopting these disclosure requirements for operating companies. These modifications include:

- Elimination of the component of the definition of a code of ethics requiring the code to promote the avoidance of conflicts of interest, including disclosure to an appropriate person or persons identified in the code of any material transaction or relationship that reasonably could be expected to give rise to such a conflict;[51]
- Addition of an instruction to indicate that a company may have separate codes of ethics for different types of officers and that the provisions of the company's code of ethics that address the elements listed in the definition and apply to those officers may be part of a broader code that addresses additional issues and applies to additional persons;[52]
- Allowing a company to choose among three alternative methods of making their ethics codes publicly available, including:

(i) Filing a copy of the code as an exhibit to its annual report on Form N–CSR or Form N–SAR;

(ii) Posting the text of the code on the company's Internet website and disclosing, in its most recent report on Form N–CSR or Form N–SAR, its Internet address and the fact that it has posted the code of ethics on its Internet website; or

(iii) Providing an undertaking in the company's most recent report on Form N–CSR or Form N–SAR to provide a copy of the code to any person without charge upon request, and explaining the manner in which such a request may be made;[53]

- Extension of the deadline for disclosing any amendments to, or waivers from, the company's code of ethics on its Internet website from two business days to five business days after the amendment or waiver;[54]
- Clarification that only amendments to, and waivers from, a company's code relating to specified elements of the code and specified officers must be disclosed;[55]
- Addition of a definition of the terms ''waiver'' and ''implicit waiver';[56] and
- Clarification that a company does not need to disclose technical, administrative, or other non-substantive amendments to its code of ethics.[57]

These disclosure requirements will apply to all registered management investment companies, regardless of whether they are required to file reports pursuant to Section 13(a) or 15(d) of the Exchange Act. Management investment companies other than SBICs will provide the required disclosure in Item 2 of Form N–CSR, and SBICs will provide the required disclosure as an exhibit to Form N–SAR.[58]

Several commenters suggested that the code of ethics requirements should not apply to any registered investment companies. These commenters argued that the proposed amendments were unnecessary and potentially duplicative, noting that investment companies are already required to disclose whether they have a code of

[46] Rule 12b–25(a) and (b)(2)(ii) under the Exchange Act [17 CFR 240.12b–25(a) and (b)(2)(ii)] and Exchange Act Form 12b–25 [17 CFR 249.322].

[47] *See* Section II.B., ''Code of Ethics,'' in Section 406/407 Adopting Release, *supra* note 8.

[48] Item 2(a) of Form N–CSR; Instruction 102P3(a)(1) of Form N–SAR.

[49] *Id.*

[50] Items 2(c), 2(d), and 2(e), and Instruction 3 to Item 2, of Form N–CSR; Instructions 102P3(a)(3), (a)(4), (a)(5), and (a)(9) of Form N–SAR.

[51] Item 2(b) of Form N–CSR; Instruction 102P3(a)(2) of Form N–SAR; Section II.B.2.c., ''Final Definition of 'Code of Ethics,' '' in Section 406/407 Adopting Release, *supra* note.

[52] Instruction 1 to Item 2 of Form N–CSR; Instruction 102P3(a)(7) of Form N–SAR; Section II.B.2.c., ''Final Definition of 'Code of Ethics,' '' in Section 406/407 Adopting Release, *supra* note 8.

[53] Item 2(f) of Form N–CSR; Instruction 102P3(a)(6) of Form N–SAR; Section II.B.3, ''Filing of Ethics Code as an Exhibit,'' in Section 406/407 Adopting Release, *supra* note 8. Because Forms N–CSR and N–SAR are filed semi-annually, unlike Forms 10–K and 10–KSB for operating companies, our rules require disclosure of the intention to provide Internet disclosure of the code of ethics, or the undertaking to provide a copy of the code of ethics to any person upon written request, in the investment company's most recently filed semi-annual report on Form N–CSR or N–SAR.

[54] Instruction 3 to Item 2 of Form N–CSR; Instruction 102P3(a)(9) of Form N–SAR; Section II.B.5, ''Form 8–K or Internet Disclosure Regarding Changes to, or Waivers from, the Code of Ethics,'' in Section 406/407 Adopting Release, *supra* note 8.

[55] Items 2(c) and 2(d) of Form N–CSR; Instructions 102P3(a)(3) and (a)(4) of Form N–SAR; Section II.B.5, ''Form 8–K or Internet Disclosure Regarding Changes to, or Waivers from, the Code of Ethics,'' in Section 406/407 Adopting Release, *supra* note.

[56] Instruction 5 to Item 2 of Form N–CSR; Instruction 102P3(a)(11) of Form N–SAR; Section II.B.5, ''Form 8–K or Internet Disclosure Regarding Changes to, or Waivers from, the Code of Ethics,'' in Section 406/407 Adopting Release, *supra* note 8.

[57] Instruction 4 to Item 2 of Form N–CSR; Instruction 102P3(a)(10) of Form N–SAR; ''Form 8–K or Internet Disclosure Regarding Changes to, or Waivers from, the Code of Ethics,'' in Section 406/407 Adopting Release, *supra* note 8.

[58] Item 2 of Form N–CSR; Instruction 102P3(a) of Form N–SAR.

ethics pursuant to rule 17j–1 under the Investment Company Act, and that in any event, investment companies are highly regulated under the Investment Company Act, which addresses the underlying ethical concerns substantively rather than simply through disclosure.[59]

We continue to believe, however, that the rule should apply with equal force to investment companies and operating companies, and we note that the Sarbanes-Oxley Act does not distinguish between them with respect to the code of ethics requirements. We recognize that rule 17j–1 currently requires investment companies, and their investment advisers and principal underwriters, to adopt codes of ethics designed to prevent fraud resulting from personal trading in securities by portfolio managers and other employees. The amendments we are adopting today, however, will address a broader range of conduct, including disclosure provided in filings with the Commission; compliance with governmental laws, rules, and regulations; and ethical conduct generally, including the ethical handling of actual or apparent conflicts of interest.[60]

The rules we are adopting will require disclosure of an investment company's code of ethics that applies to its principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions, regardless of whether these individuals are employed by the investment company or a third party.[61] Our proposed rules would also have required disclosure of certain codes of ethics of an investment company's investment adviser and principal underwriter that apply to the adviser's and underwriter's principal executive officer and senior financial officers.[62]

We are persuaded by commenters that including codes of ethics of the investment adviser and principal underwriter goes beyond the intended scope of Section 406. In large financial services organizations, the principal executive officer and senior financial officers may have little to do with the operations or financial reporting of the investment company, but are instead responsible principally for the adviser's or underwriter's own operations and financial reporting.

In addition, we have determined to exclude UITs from the code of ethics disclosure requirements. Because UITs are unmanaged, passive investment companies, they typically do not have principal executive officers, principal financial officers, principal accounting officers or controllers, or persons performing similar functions. In light of the fact that we have limited the rules we are adopting to these persons, we believe that it is appropriate to exclude UITs from the disclosure requirements. We note that we have provided a similar exclusion to issuers of asset-backed securities.[63]

C. Section 407 of the Sarbanes-Oxley Act—Audit Committee Financial Experts

We are adopting, with modifications to address commenters' concerns, our proposals that implement Section 407 of the Sarbanes-Oxley Act with respect to registered management investment companies. These requirements are similar to those that we recently adopted for operating companies, and we direct investment companies to that release for guidance concerning these requirements.[64] Under the provisions that we are adopting, a registered management investment company must disclose annually that its board of directors has determined that the company either: (i) Has at least one ''audit committee financial expert'' serving on its audit committee, and if so, the name of the expert and whether the expert is ''independent'; or (ii) does not have an audit committee financial expert serving on its audit committee. An investment company disclosing that it does not have an audit committee financial expert must explain why it does not have such an expert.[65]

The rules, as adopted, reflect modifications that are similar to those that we recently made to the proposed financial expert disclosure requirements for operating companies, for the reasons described in the release adopting these disclosure requirements for operating companies. These modifications include:

- Use of the term ''audit committee financial expert'' rather than ''financial expert;''[66]
- Modification of the proposals that would have required disclosure of the number and names of audit committee financial experts serving on a company's audit committee to more closely track the language used in Section 407 of the Sarbanes-Oxley Act, and to require a company to disclose that its board of directors has determined that the company either has at least one audit committee financial expert serving on its audit committee or does not have an audit committee financial expert serving on its audit committee;[67]
- Modification of the proposals to permit, but not require, an investment company to disclose that it has more than one audit committee financial expert on its audit committee. Therefore, once an investment company's board determines that a particular audit committee member qualifies as an audit committee financial expert, it may, but is not required to, determine whether additional audit committee members also qualify as experts. Every investment company subject to the audit committee disclosure requirements would, however, have to determine whether or not it has at least one audit committee financial expert; a company will not satisfy the new disclosure requirements by stating that it has decided not to make a determination or by simply disclosing the qualifications of all of its audit committee members. Furthermore, if the company's board determines that at least one of the audit committee members qualifies as an expert, the company must accurately disclose this fact. It will not be appropriate for a company to disclose that it does not have an audit committee financial expert if its board has determined that

[59] 17 CFR 270.17j–1.

[60] General Instruction D to Form N–CSR permits a registered management investment company to incorporate its code of ethics by reference from another document, such as its registration statement. *See* Item 23(p) of Form N–1A; Item 24.2.r of Form N–2; Item 28(b)(17) of Form N–3 (requiring codes of ethics required by rule 17j–1 to be filed as exhibits to registration statements).

[61] Item 2 of Form N–CSR; Instruction 102P3(a) of Form N–SAR.

[62] Section 406/407 Proposing Release, *supra* note, 67 FR at 66217.

[63] *See* Instruction 3 to Item 406 of Regulation S–K [17 CFR 229.406]; Section II.D., ''Asset-Backed Issuers,'' in Section 406/407 Adopting Release, *supra* note 8.

[64] *See* Section II.A, ''Audit Committee Financial Experts,'' in Section 406/407 Adopting Release, *supra* note 8.

[65] Registered management investment companies other than SBICs will be required to provide the audit committee financial expert disclosure in Item 3 of Form N–CSR. SBICs will be required to provide this disclosure in an exhibit to Form N–SAR, pursuant to Instruction 102P3(b) of Form N–SAR (SBICs).

[66] Item 3 of Form N–CSR; Instruction 102P3(b) of Form N–SAR; Section II.A.1, ''Title of the Expert,'' in Section 406/407 Adopting Release, *supra* note 8. Throughout this release, we refer to both ''audit committee financial experts'' and ''financial experts'' as appropriate in a particular context. For example, when discussing statutory provisions, we refer to ''financial experts.'' For purposes of the discussions in this release, the meanings of these terms are identical.

[67] Item 3(a)(1) of Form N–CSR; Instruction 102P3(b)(1) of Form N–SAR; Section II.A.2, ''Disclosure of the Number and Names of Audit Committee Financial Experts,'' in Section 406/407 Adopting Release, *supra* note 8.

such an expert serves on the audit committee;[68]

• Reorganization of the components of the definition of audit committee financial expert to make it easier to read and to emphasize, by including them in the first part of the definition, the attributes that an audit committee financial expert must possess;[69]

• Revision of the second attribute to state that the audit committee financial expert must have the ability to assess the general application of generally accepted accounting principles in connection with the accounting for estimates, accruals, and reserves, rather than stating that the expert must have experience applying these principles;[70]

• Broadening of the third attribute by requiring an audit committee financial expert to have experience ''preparing, auditing, analyzing, or evaluating'' financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of issues that can reasonably be expected to be raised by the registrant's financial statements, or experience actively supervising a person who prepares, audits, analyzes or evaluates financial statements;[71]

• Modification of the fourth attribute to require understanding of, rather than experience with, internal controls and procedures for financial reporting;[72]

• Modification of the definition to state that a person must have acquired the five necessary attributes through any one or more of the following: (i) Education and experience as a principal financial officer, principal accounting officer, controller, public accountant, or auditor or experience in one or more positions that involve the performance of similar functions; (ii) experience actively supervising a principal financial officer, principal accounting officer, controller, public accountant, auditor, or person performing similar functions; (iii) experience overseeing or assessing the performance of companies or public accountants with respect to the preparation, auditing, or evaluation of financial statements; or (iv) other relevant experience.[73]

• Elimination of the requirement that an audit committee financial expert must have gained the relevant expertise with a company that was required to file reports pursuant to Section 13(a) or 15(d) of the Exchange Act;[74]

• Addition of a requirement that if a person qualifies as an audit committee financial expert by virtue of possessing ''other relevant experience,'' the company's disclosure briefly list that person's experience;[75]

• Elimination of the list of factors that a company's board of directors should consider in evaluating the education and experience of an audit committee financial expert candidate;[76] and

• Addition of a safe harbor in the audit committee disclosure requirements.[77]

We wish to emphasize that, as with an operating company, the board of an investment company must ensure that it names an audit committee financial expert who embodies the highest standards of personal and professional integrity. In this regard, a board should consider any disciplinary actions to which a potential expert is, or has been, subject in determining whether that person would be a suitable audit committee financial expert.[78]

The disclosure requirements that we are adopting will apply to all registered management investment companies, regardless of whether they are required to file reports under Section 13(a) or 15(d) of the Exchange Act. Several commenters objected to our proposal to require a registered management investment company to provide disclosure about audit committee financial experts serving on its audit committee. They argued that investment companies should be excluded entirely from any disclosure requirement relating to audit committee financial experts, because the nature of investment company accounting is such that investment company audit committees rarely are required to apply complex accounting principles. These commenters stated that the preparation of investment company financial statements is straightforward and does not present the types of circumstances that require the exercise of judgment, such as selection of accounting policies, that preparation of the financial statements of operating companies would.

We continue to believe, however, that the rule should apply with equal force to investment companies and operating companies, and we note that the Sarbanes-Oxley Act does not distinguish between them with respect to the financial expert disclosure requirements. In addition, while investment company financial statements may, in many cases, be simpler than those of some operating companies, the underlying financial systems, reporting mechanisms, and internal controls are sufficiently complex that an investment company's audit committee would benefit from having one or more members who meet the definition of audit committee financial expert. Finally, we note that the modifications that we have made to the definition of an audit committee financial expert should address the concerns of commenters that the definition was too narrowly drawn to apply in the context of investment companies. The commenters argued, in particular, that the second, third, and fourth required attributes were too restrictive, and that experience as a public accountant or auditor, or principal financial officer, controller, or public accounting officer of a company should not be the exclusive means for acquiring the attributes. As described above, we have made changes that are responsive to these concerns.

[68] Instruction 2 to Item 3(a) of Form N–CSR; Instruction 102P3(b)(5) of Form N–SAR; Section II.A.2, ''Disclosure of the Number and Names of Audit Committee Financial Experts,'' in Section 406/407 Adopting Release, *supra* note.

[69] Items 3(b) and 3(c) of Form N–CSR; Instructions 102P3(b)(6) and (b)(7) of Form N–SAR; Section II.A.4.d., ''Discussion of Significant Modifications to the Proposed Definition of ''Financial Expert,''' in Section 406/407 Adopting Release, *supra* note 8.

[70] Item 3(b)(2) of Form N–CSR; Instruction 102P3(b)(6)(ii) of Form N–SAR; Section II.A.4.d.(ii), ''Discussion of Significant Modifications to the Proposed Definition of ''Financial Expert,''' in Section 406/407 Adopting Release, *supra* note.

[71] Item 3(b)(3) of Form N–CSR; Instruction 102P3(b)(6)(iii) of Form N–SAR; Section II.A.4.d., ''Discussion of Significant Modifications to the Proposed Definition of ''Financial Expert,''' in Section 406/407 Adopting Release, *supra* note 8. By active supervision, we do not simply mean that a traditional hierarchical reporting relationship exists between supervisor and those being supervised. Rather, we mean that a person engaged in active supervision addresses, albeit at a supervisory level, the same general types of issues regarding preparation, auditing, analysis, or evaluation of financial statements as those addressed by the person or persons being supervised.

[72] Item 3(b)(4) of Form N–CSR; Instruction 102P3(b)(6)(iv) of Form N–SAR; Section II.A.4.d., ''Discussion of Significant Modifications to the Proposed Definition of ''Financial Expert,''' in Section 406/407 Adopting Release, *supra* note 8.

[73] Item 3(c) of Form N–CSR; Instruction 102P3(b)(7) of Form N–SAR; Section II.A.4.d., ''Discussion of Significant Modifications to the Proposed Definition of ''Financial Expert,''' in Section 406/407 Adopting Release, *supra* note 8.

[74] Item 3(c) of Form N–CSR; Instruction 102P3(b)(7) of Form N–SAR; Section II.A.4.d., ''Discussion of Significant Modifications to the Proposed Definition of ''Financial Expert,''' in Section 406/407 Adopting Release, *supra* note 8.

[75] Instruction to Item 3 of Form N–CSR; Instruction 102P3(b)(9) of Form N–SAR.

[76] Section II.A.4.d., ''Discussion of Significant Modifications to the Proposed Definition of ''Financial Expert,''' in Section 406/407 Adopting Release, *supra* note 8.

[77] Item 3(d) of Form N–CSR; Instruction 102P3(b)(8) of Form N–SAR; Section II.A.5, ''Safe Harbor from Liability for Audit Committee Financial Experts,'' in Section 406/407 Adopting Release, *supra* note 8.

[78] Section II.A.4.d., ''Discussion of Significant Modifications to the Proposed Definition of ''Financial Expert,''' in Section 406/407 Adopting Release, *supra* note 8.

We are adopting, substantially as proposed, a test for whether an audit committee financial expert may be considered to be ''independent'' that differs from the test we have adopted for operating companies. The definition of ''independence'' adopted for operating companies refers to the definition of ''independent'' used in Item 7(d)(3)(iv) of Schedule 14A, which generally is not applicable to investment companies.[79] Under the rules we are adopting, in order to be considered ''independent,'' a member of an audit committee of a registered management investment company may not, other than in his or her capacity as a member of the audit committee, the board of directors, or any other board committee: (i) Accept directly or indirectly any consulting, advisory, or other compensatory fee from the issuer; or (ii) be an ''interested person'' of the investment company, as defined in Section 2(a)(19) of the Investment Company Act.[80]

III. Transition Provisions and Compliance Dates

Except as provided in the following sentence, the effective date of the rules, rule and form amendments, and Form N–CSR is March 1, 2003. The effective date of the removal of the certification requirement from Form N–SAR for registered management investment companies other than SBICs is May 1, 2003.

A registered management investment company other than an SBIC that has a fiscal annual or semi-annual period ending on or before March 31, 2003, may choose either to file Form N–CSR or to continue to comply with the certification requirements of Form N–SAR. A registered management investment company that elects to file Form N–CSR for a fiscal annual or semi-annual period ending on or before March 31, 2003, is not required to comply with paragraphs (b)(4), (5), and (6) of Investment Company Act Rule 30a-2, Item 9(a) of Form N–CSR, or paragraph (b) of Exchange Act Rules 13a-15 and 15d-15 and Investment Company Act Rule 30a-3 with respect to that Form N–CSR. A registered management investment company that elects to certify Form N–SAR for a fiscal annual or semi-annual period ending on or before March 31, 2003, must file its report to shareholders for that period as currently required. This transition is designed so that each such registered management investment company other than an SBIC will be required to provide a certification of its financial statements and financial information, while providing the flexibility to each company to determine whether to certify Form N–SAR or Form N–CSR during the transition period and sufficient time to establish and evaluate disclosure controls and procedures for Form N–CSR. A registered management investment company other than an SBIC that has a fiscal annual or semi-annual period ending on or after April 1, 2003, is required to file Form N–CSR for that period. Beginning immediately, a unit investment trust or an SBIC may omit the certification from Form N–SAR.

Registered management investment companies must comply with the code of ethics disclosure requirements promulgated under Section 406 of the Sarbanes-Oxley Act in their annual reports on Form N–CSR or N–SAR for fiscal years ending on or after July 15, 2003. They also must comply with the requirements regarding disclosure of amendments to, and waivers from, their ethics codes on or after the date on which they file their first annual report on Form N–CSR or N–SAR in which disclosure of their code of ethics is required. Registered management investment companies similarly must comply with the audit committee financial expert disclosure requirements promulgated under Section 407 of the Sarbanes-Oxley Act in their annual reports on Form N–CSR or N–SAR for fiscal years ending on or after July 15, 2003.

IV. Paperwork Reduction Act

The new rules and rule and form amendments contain ''collection of information'' requirements within the meaning of the Paperwork Reduction Act of 1995 (''PRA'').[81] We published notice requesting comment on the collection of information requirements in the release proposing Form N–CSR,[82] submitted these requirements to the Office of Management and Budget (''OMB'') for review in accordance with the PRA,[83] and received approval by OMB for this collection of information. In addition, we published notice requesting comment on the collection of information requirements in the proposing release implementing Sections 406 and 407 of the Sarbanes-Oxley Act[84] and submitted these requirements to OMB for review. This request is pending before OMB.

The titles for the collection of information are ''Form N–CSR under the Investment Company Act of 1940 and Securities Exchange Act of 1934, Certified Shareholder Report;'' ''Form N–SAR under the Investment Company Act of 1940, Semi-Annual Report for Registered Investment Companies;'' and ''Form 12b–25 under the Securities Exchange Act of 1934, Notification of Late Filing.''

Form N–SAR (OMB Control No. 3235–0330) under the Exchange Act and the Investment Company Act [17 CFR 249.330; 17 CFR 274.101] is used by registered investment companies to file periodic reports with the Commission. Form N–CSR (OMB Control No. 3235–0570) under the Exchange Act and the Investment Company Act [17 CFR 249.331; 17 CFR 274.128] will be used by registered management investment companies to file certified shareholder reports. Form 12b–25 (OMB Control No. 3235–0058) under the Exchange Act [17 CFR 249.322] provides notice to the Commission and the marketplace that a company will be unable to file a required report in a timely manner.

Compliance with the new rules and rule and form amendments is mandatory and the information provided will not be kept confidential. Under our rules for retention of manual signatures, registered investment companies have to maintain the certifications for five years.[85] An agency may not conduct or sponsor, and a person is not required to respond to, an information collection unless it displays a currently valid OMB control number.

A. Summary of New Rules

On August 28, 2002, the Commission implemented the certification requirement of Section 302 of the Sarbanes-Oxley Act with respect to registered investment companies by adopting new rule 30a–2 under the Investment Company Act and the Sarbanes-Oxley Act.[86] Rule 30a–2 requires a registered investment company that files periodic reports under Section 13(a) or 15(d) of the Exchange Act, *i.e.*, Form N–SAR, to include the certification specified by Section 302 in those periodic reports.

In a companion release, we also proposed to require registered management investment companies to file certified shareholder reports with the Commission on new Form N–CSR

[79] *See* Item 7(d)(3)(vii) of Schedule 14A [17 CFR 240.14a-101] (providing that a registered investment company, other than a closed-end investment company, need not provide the information required by Item 7(d)(3) about its audit committee).

[80] Item 3(a)(2) of Form N–CSR; Instruction 102P3(b)(2) of Form N–SAR.

[81] 44 U.S.C 3501 *et seq.*

[82] Form N–CSR Proposing Release, *supra* note 5.

[83] 44 U.S.C. 3507(d) and 5 CFR 1320.11.

[84] Investment Company Act Release No. 25775 (Oct. 22, 2002) [67 FR 66208 (Oct. 30, 2002)].

[85] *See* Rule 302(b) of Regulation S–T [17 CFR 232.302(b)].

[86] Investment Company Act Release No. 25722 (Aug. 28, 2002) [67 FR 57276 (Sept. 9, 2002)].

and to designate these certified shareholder reports as reports that are required under Sections 13(a) and 15(d) of the Exchange Act and Section 30 of the Investment Company Act.[87] As we noted in that release, we believe that the certification requirement of Section 302 of the Sarbanes-Oxley Act was intended to improve the quality of the disclosure that a company provides regarding its financial condition in its reports to investors.[88] For registered management investment companies, the required reports to shareholders, rather than reports on Form N–SAR, are the primary vehicle for providing financial information to investors. We believe that the information in these reports to shareholders should be certified, and we are adopting amendments to our forms and rules to require this certification.

We are adopting an amendment to rule 30b2–1 under the Investment Company Act, which will require a registered management investment company to file a report with the Commission on new Form N–CSR containing (i) a copy of any required shareholder report, (ii) additional information regarding disclosure controls and procedures, and (iii) the certification required by the Sarbanes-Oxley Act.[89] New rule 30d–1 designates certified shareholder reports on Form N–CSR as periodic reports under Section 13(a) or 15(d) of the Exchange Act.[90] New rule 30a–3 requires all registered management investment companies to maintain, and regularly evaluate the effectiveness of, disclosure controls and procedures designed to ensure that the information required in filings under the Exchange Act is recorded, processed, summarized, and reported on a timely basis. We are also amending the definition of ''disclosure controls and procedures'' in rule 30a–2(c) to make clear that such controls and procedures apply to all registered management investment companies regardless of whether they are required to file reports on Form N–CSR under the Exchange Act, and that they do not apply to SBICs and UITs filing Exchange Act reports on Form N–SAR.[91] Amendments to Exchange Act rules 13a–15 and 15d–15 will exclude SBICs and UITs from the requirements to maintain disclosure controls and procedures for purposes of the evaluation conducted as part of the required certification.[92] We are also removing the requirement that Form N–SAR be certified by a registered investment company's principal executive and financial officers. This shifts the information collection burden relating to the certification specified by Section 302 of the Sarbanes-Oxley Act, for registered management investment companies, from Form N–SAR to Form N–CSR.

Finally, we are requiring registered management investment companies to include new disclosures on Form N–CSR or Form N–SAR, as appropriate, in order to implement the requirements of Sections 406 and 407 of the Sarbanes-Oxley Act of 2002. First, the rules require a management investment company to disclose whether it has at least one ''audit committee financial expert'' serving on its audit committee, and if so, the name of the expert and whether the expert is independent of management. A management investment company that does not have an audit committee financial expert must disclose this fact and explain why it has no such expert. Second, the rules require a management investment company to disclose whether it has adopted a code of ethics that applies to the company's principal executive officer and senior financial officers, or persons performing similar functions, regardless of whether they are employed by the management investment company or a third party. A management investment company disclosing that it has not adopted such a code must disclose this fact and explain why it has not done so. A management investment company also will be required to disclose amendments to, and waivers from, the code of ethics relating to any of those officers.

All of these new rules and rule amendments are part of the collection of information of new Form N–CSR or Form N–SAR (in the case of SBICs) because Form N–CSR contains the requirement that each registered management investment company filing reports on this form has to certify the contents of the report, and Form N–CSR and Form N–SAR contain the requirement that management investment companies must provide the appropriate audit committee financial expert and code of ethics disclosures.

We are amending our rules and forms to provide that, for registered management investment companies other than small business investment companies, Form N–SAR will be filed under the Investment Company Act only and not the Exchange Act.[93] Also, we have amended Form N–SAR to eliminate the requirement that UITs and SBICs certify their reports on Form N–SAR.[94] We are also adopting amendments to require an investment company to file a Form 12b-25 if it will not be able to file a report on Form N–CSR in a timely manner.[95]

B. Reporting and Cost Burden Estimates

Certification of Form N–CSR

The reporting burden associated with the certification requirement requires the principal executive and financial officer to review and analyze each periodic report to be filed by an investment company in order to make the required certification. In the release proposing Form N–CSR, we estimated a total of five burden hours per respondent for the certification and asked for comment on this estimate.[96] We received three comment letters specifically discussing our estimate of the burden for filing and certifying Form

[87] *See* Form N–CSR Proposing Release, *supra* note 5.

A management investment company is an investment company other than a unit investment trust or face-amount certificate company. *See* Section 4 of the Investment Company Act [15 U.S.C. 80a–4]. Management investment companies typically issue shares representing an undivided proportionate interest in a changing pool of securities, and include open-end and closed-end companies. *See* T. Lemke, G. Lins, A. Smith III, Regulation of Investment Companies, Vol. I, ch. 4, § 4.04, at 4–5 (2002).

[88] Form N–CSR Proposing Release, *supra* note 5, 67 FR at 57299.

[89] Rule 30b2–1(a) under the Investment Company Act [17 CFR 270.30b2–1(a)]; Items 1, 9, and 10(b). In addition, we are amending rule 30a–2 under the Investment Company Act [17 CFR 270.30a–2] to require Form N–CSR to include the certification required by Section 302 of the Sarbanes-Oxley Act.

[90] We are also adopting a technical conforming amendment that would delete the language in current rule 30a–1 [17 CFR 270.30a–1] stating that a registered management investment company required to file an annual report pursuant to Section 13(a) or 15(d) of the Exchange Act and Section 30(a) of the Investment Company Act shall be deemed to have satisfied its requirement to file an annual report by the filing of semi-annual reports on Form N–SAR. The amendments rename rule 30a–1 in order to specify that it relates to annual reports by registered unit investment trusts, and rename rule 30b1–1 [17 CFR 270.30b1–1] in order to specify that it relates to semi-annual reports of registered management investment companies.

[91] Rule 30a–2(c) under the Investment Company Act [17 CFR 270.30a–2].

[92] 17 CFR 240.13a–15(a); 17 CFR 240.15d–15(a).

[93] *See* Rule 30b1–1 under the Investment Company Act [17 CFR 270.30b1–1]; and General Instruction A to Form N–SAR [17 CFR 274.101]. In addition, we are adopting technical conforming amendments to rule 30b1–3 [17 CFR 270.30b1–3] to remove the reference to Form N–SAR.

[94] Instruction 102P3 of Form N–SAR; Instruction to Item 133 of Form N–SAR.

[95] Rule 12b-25(a) and (b)(2)(ii) under the Exchange Act [17 CFR 240.12b-25(a) and (b)(2)(ii)] and Exchange Act Form 12b-25 [17 CFR 249.322]. There is no collection of information for the amendments to rule 12b-25 because they are attributed to Form 12b-25.

[96] This estimate is based on the estimate of the burden of certification with respect to operating companies. *See* Investment Company Act Release No. 25722, *supra* note, 67 FR at 57284 (estimating PRA burden of certification of Forms 10–K, 10–KSB, 10–Q, 10–QSB, 20–F, and 40–F at five hours per form).

N–CSR. Two commenters claimed that our estimate was too low, because it did not reflect the fact that investment companies often have multiple portfolios. We note that our estimate already takes into account that many registered management investment companies have multiple portfolios. Our estimate of the hour burden required for operating companies to certify their reporting forms, such as Form 10–K, is similar to our estimate of the burden for investment companies.[97] While reports on Form N–CSR will contain financial statements for multiple portfolios, investment company financial statements are generally much simpler than operating company financial statements, and operating company reporting forms, such as Form 10–K, contain much information (*i.e.*, Management's Discussion and Analysis) that Form N–CSR will not contain. Based on the comments, however, we have revised our estimate, to estimate that the certification requirement required by Section 302 of the Sarbanes-Oxley Act will result in an increase of five burden hours per registrant per filing and an additional 0.5 hours per additional portfolio in connection with the certification of annual and semi-annual reports on Form N–CSR.[98]

Audit Committee Financial Expert

The amendments will increase the burden of completing Form N–CSR and Form N–SAR by requiring a management investment company to disclose whether it has at least one ''audit committee financial expert'' serving on its audit committee, and if so, the name of the expert and whether the expert is independent of management. A management investment company that does not have an audit committee financial expert must disclose this fact and explain why it has no such expert. In the release proposing these amendments, we estimated that the disclosure regarding audit committee financial experts would increase the annual burden of completing Form N–CSR or Form N–SAR by 0.5 hours per registered management investment company. We received no comments on this estimate. We believe the additional burden of these amendments would be limited, because they will not require any investment company to add an ''audit committee financial expert'' to its board. We estimate that the disclosure requirements regarding audit committee financial experts will result in an incremental increase of 0.5 burden hours per registrant per year in connection with preparing each annual report on Form N–CSR or Form N–SAR.[99] Management investment companies (other than SBICs) will have to provide this disclosure on Form N–CSR; SBICs will have to provide this disclosure on Form N–SAR.

Codes of Ethics

The amendments will require a registered management investment company to disclose whether it has adopted a written code of ethics for its principal executive officer, principal financial officer, principal accounting officer or controller, or persons serving similar functions, and file the code as an exhibit to Form N–CSR or Form N–SAR. An investment company disclosing that it has not adopted such a code must disclose this fact and explain why it has not done so. In the release proposing these amendments, we estimated that the disclosure regarding code of ethics would increase the annual burden by 0.5 hours per registered management investment company. We believe that the additional burden of these amendments would be limited, because they will not require any company to adopt such a code of ethics. Management should be readily able to determine whether or not its company has adopted a code of ethics. In certain cases, the required disclosure would require minimal analysis regarding why the company does not have a code. In addition, in the first year, registrants must file a copy of the code with the Commission. We estimate that the disclosure requirements regarding codes of ethics will also result in an incremental increase of 0.5 burden hours per registrant in connection with each annual report on Form N–CSR or Form N–SAR.[100] Management investment companies (other than SBICs) will have to make this disclosure on Form N–CSR; SBICs will have to make this disclosure on Form N–SAR.

Form N–SAR

The amendments remove the certification requirement from Form N–SAR and shift the burden of this requirement, for PRA purposes, to Form N–CSR. We estimate that about 4,500 registrants, including 3,702 management investment companies (including 2 SBICs), and 798 UITs, currently file reports on Form N–SAR. Based on an increase of 2 burden hours relating to audit committee financial experts and codes of ethics disclosure [101] and a decrease of 41,010 burden hours relating to the removal of the certification of Form N–SAR,[102] we estimate that, in the aggregate, all respondents will have an incremental decrease of 41,008 burden hours associated with Form N–SAR to comply with the new rules and rule and form amendments.

Form N–CSR

We estimate that about 3,700 registrants will file Form N–CSR. Based on Commission experience with reporting forms in general and other related rules, we estimate that approximately 75% of the added burden hours will be expended by internal staff for internal review and the remaining 25% will be for outside legal costs associated with reviewing the new disclosures at a cost of $300 per hour.[103] Based on the burden hour estimate for the certification of Form N–CSR, the disclosure related to an audit committee financial expert, and the disclosure related to the code of ethics, we estimate that, in the aggregate, all respondents will incur an incremental increase of

[97] Investment Company Act Release No. 25722, *supra* note, 67 FR at 57284 (estimating PRA burden of certification of Forms 10–K, 10–KSB, 10–Q, 10–QSB, 20–F, and 40–F at five hours per form).

[98] Currently, the estimated total burden for the certification requirement of Form N–CSR is 37,000 hours, reflecting an estimate of 3,700 management investment companies filing twice a year and an estimate of five hours per filing. In response to comments, we are increasing this estimate by 6,150 hours to reflect the additional burden for certification of multiple portfolios. We calculate 6,150 hours as follows: We estimate that there are 9,850 total portfolios of registered management investment companies. This reflects 6,150 additional series (*i.e.*, series beyond the first series or the 3,700 series already accounted for in the burden estimate) of multiple series funds filing twice a year and 0.5 hours per additional series per filing. Based on our experience with reporting forms in general, we estimate that the incremental burden hours of reviewing financial statements for other series will be relatively limited because many series may be able to use the same certification process for many of the items (*i.e.*, disclosure controls and procedures). This new requirement will result in a new total of 43,150 burden hours for the certification requirement of Form N–CSR.

[99] We estimate the total new burden for this disclosure requirement to be 1,851 hours. ((0.5 hours × 3,700 management investment companies other than SBICs) + (0.5 hours × 2 SBICs) = 1,851 hours).

[100] We estimate the total new burden for this disclosure requirement to be 1,851 hours. (0.5 hours × 3,700 management investment companies other than SBICs) + (0.5 hours × 2 SBICs) = 1,851 hours.

[101] This estimate includes 1 hour for the audit committee financial expert disclosure (0.5 hours x 2 SBICs) and 1 hour for the code of ethics disclosure (0.5 hours × 2 SBICs).

[102] (3,702 management companies (including SBICs) × 10 hours annually) + (798 UITs × 5 hours annually) = 41,010 hours.

[103] These percentages are based on consultations with several issuers, law firms and other persons who regularly assist issuers in preparing and filing reports with the Commission. We have used an estimated hourly rate of $300.00 to determine the estimated cost to issuers of having the required disclosures reviewed by outside counsel. We arrived at this hourly rate estimate based on consultations with several private law firms.

35,139 burden hours [104] and $3,513,900 in outside legal costs [105] to comply with the new rules and rule and form amendments.

Form 12b–25

Form 12b–25 provides notice to the Commission and the marketplace that registrants will be unable to file a required report in a timely manner. If certain conditions are met, the registrant will be granted an automatic filing extension. The proposed amendments would permit investment companies to use Form 12b–25 for the purpose of obtaining extensions with respect to filing Form N–CSR. We estimate that an average of 168 investment companies per year use Form 12b–25 to obtain extensions of time for filing Form N–SAR spending, on average, approximately 2.5 hours completing the form. We estimate that the same number of investment companies, though not necessarily the same specific investment companies, will also use Form 12b–25 to obtain extensions of filing Form N–CSR annually, resulting in an incremental increase of 420 burden hours [106] to comply with the new rules and form and form and rule amendments.

V. Cost-Benefit Analysis

The Commission is sensitive to the costs and benefits imposed by its rules. Our rules and rule and form amendments more fully implement Section 302 of the Sarbanes-Oxley Act by requiring a registered management investment company, other than a small business investment company (''SBIC''), to file certified shareholder reports with the Commission on Form N–CSR containing (i) a copy of any required report to shareholders, (ii) additional information regarding disclosure controls and procedures, and (iii) the certification required by Section 302 of the Sarbanes-Oxley Act. These amendments also will designate certified shareholder reports on Form N–CSR, filed by management investment companies, as periodic reports filed with the Commission under the Exchange Act. Therefore, these amendments will require the certification of each management investment company's principal executive and financial officer to be included in its certified shareholder reports on Form N–CSR. We also are amending the instructions to Form N–SAR, the semi-annual reporting form for registered investment companies, to remove the certification requirement from the form and designate it as an Investment Company Act only filing for registered management investment companies other than SBICs. Further, we are amending Form 12b–25 to permit investment companies to use Form 12b–25 for the purpose of obtaining extensions with respect to filing Form N–CSR. In addition, the rules will require all registered management investment companies, other than SBICs, to maintain, and regularly evaluate the effectiveness of, disclosure controls and procedures designed to ensure that the information required in their filings on Form N–CSR is recorded, processed, summarized, and reported on a timely basis.

Finally, we are requiring registered management investment companies to include new disclosures on Form N–CSR or Form N–SAR, as appropriate, in order to implement the requirements of Sections 406 and 407 of the Sarbanes-Oxley Act of 2002. First, the rules require a management investment company to disclose whether it has at least one ''audit committee financial expert'' serving on its audit committee, and if so, the name of the expert and whether the expert is independent of management. A management investment company that does not have an audit committee financial expert must disclose this fact and explain why it has no such expert. Second, the rules require a management investment company to disclose whether it has adopted a code of ethics that applies to the company's principal executive officer and senior financial officers, or persons performing similar functions, regardless of whether they are employed by the management investment company or any third party. A management investment company disclosing that it has not adopted such a code must disclose this fact and explain why it has not done so. A management investment company also will be required to disclose amendments to, and waivers from, the code of ethics relating to any of those officers.

We received one comment letter specifically addressing this Section. The commenter urged the Commission to review its cost-benefit analysis with a view not only to the new rules but to the increased costs, such as legal and accounting fees, imposed on smaller investment companies associated with other recently adopted rules, such as anti-money laundering procedures. The purpose of this cost-benefit analysis is to focus on the costs associated only with the adoption of the rules requiring the filing of Form N–CSR. The costs associated with other recently adopted rules imposed on smaller investment companies should be discussed in the cost-benefit sections of those specific rulemakings.

A. Benefits

Certification of Form N–CSR

In adopting these new rules and rule and form amendments, we intend to more fully implement the intent of Section 302 of the Sarbanes-Oxley Act, by improving the quality of the disclosure that an investment company provides about its financial condition in its periodic reports to investors. Section 302 of the Sarbanes-Oxley Act requires the principal executive and financial officers of an issuer to certify the information contained in the issuer's quarterly or annual reports filed under Section 13(a) or 15(d) of the Exchange Act. Currently, Form N–SAR is the reporting form for registered investment companies that satisfies the filing requirement under Section 13(a) or 15(d) of the Exchange Act. Form N–SAR does not contain financial statements and is a regulatory compliance form that is not delivered to investors. Thus, the amendments will remove the certification requirement from Form N–SAR, a form that does not contain financial statements, and will impose the certification requirement on Form N–CSR, a form that contains financial statements. Requiring a registered investment company's principal executive and financial officers to file certified shareholder reports on Form N–CSR will require these officers to certify, in part, that the financial statements and other financial information contained in the report fairly present in all material respects the financial condition, results of operations, changes in net assets, and cash flows (if the financial statements are required to include a statement of cash flows) of the registered investment company.

The rules should help to ensure that registered investment companies maintain sufficient disclosure controls and procedures to provide reasonable assurance to investors that registered investment companies can record, process, summarize, and report on a timely basis information that is required on Form N–CSR, including information

[104] 43,150 hours for certification + 1,851 hours for audit committee financial expert disclosure + 1,851 hours for code of ethics disclosure = 46,852 hours x .75 = 35,139 hours.

[105] 43,150 hours for certification + 1,851 hours for audit committee financial expert disclosure + 1,851 hours for code of ethics disclosure = 46,852 hours × .25 for outside counsel × $300 per hour = $3,513,900.

[106] 168 registered investment companies × 2.5 hours = 420 burden hours.

contained in reports to shareholders.[107] To the extent that registered investment companies do not maintain adequate procedures, the rules should lead to the development, or enhancement and modernization, of these procedures. Further, the certification requirement in our rules will require an investment company under the supervision of its management to conduct an evaluation of these disclosure controls and procedures within the 90-day period prior to the filing date of each report requiring certification. This will help to ensure that registered investment companies devote adequate resources and attention to the maintenance of their reporting systems. Additionally, the required evaluation will help to ensure the continuous, orderly, and timely flow of information within the registered investment company and, ultimately, to investors.

By emphasizing the importance of the role of senior officers in the reporting process, the new rules and rule and form amendments will help to enhance investor confidence in the quality of the disclosure in registered investment companies' reports to shareholders. This, in turn, will help to encourage investor confidence in these investment companies. Even though the certification is consistent with the current obligation of officers and directors of a mutual fund not to make statements that are materially misleading, we believe that investors may benefit from the certification because the certifying officers provide additional assurance to investors that the reports that they file under the Exchange Act meet this standard. We requested comment on these benefits, but received none.

Audit Committee Financial Expert

A management investment company must disclose whether it has at least one ''audit committee financial expert'' serving on its audit committee, and if so, the name of the expert and whether the expert is independent of management. A management investment company that does not have an audit committee financial expert must disclose this fact and explain why it has no such expert. We believe that investors will benefit from this disclosure by being able to consider it when reviewing the disclosure currently required about the background and affiliations of the directors of the investment company. Investors will also benefit to the extent that having an audit committee financial expert on an audit committee of a company increases their confidence in the company. The modifications we are making to our proposal will not reduce the level of required expertise and thus will not mitigate the benefits to investor confidence of requiring this disclosure. We requested comment on these benefits, but received none.

Codes of Ethics

The requirement that investment companies file copies of their codes of ethics will allow investors to better understand the ethical principles that guide executives of companies in which they invest. Investors will also benefit to the extent that having disclosure of a code of ethics of a company increases their confidence in the company. We requested comment on these benefits, but received none.

B. Costs

While the new rules and rule and form amendments may lead to some additional costs for registered investment companies, we believe that these costs should be limited.

Certification of Form N–CSR

These amendments will require each registered management investment company's principal executive and financial officer to certify the information contained in its certified shareholder reports on Form N–CSR. In order to provide the required certification, each principal executive and financial officer will need to review these reports. We believe that these officers already review these reports, so there should be no additional burden imposed on these companies. To the extent that these officers would need to spend additional time critically reviewing the overall context of the disclosure provided in these reports, the company would incur costs which are difficult for us to quantify.

We believe that most registered management investment companies already maintain some form of disclosure controls and procedures for identifying and processing the information needed to satisfy their disclosure obligations to their shareholders. The amendments do not dictate that registered investment companies follow any particular procedure. Alternatively, we could have required specific controls and procedures for all investment companies. By allowing management investment companies to determine what procedures are necessary to meet the obligations of the new rules, the Commission is mitigating the costs associated with compliance. Some registered management investment companies may need to institute appropriate procedures while others may need to enhance existing informal or ad hoc procedures. These incremental costs are difficult to quantify. We do not have data to quantify the cost of implementing, or upgrading and strengthening existing, internal reporting procedures.

The requirement in the certification that disclosure controls and procedures be evaluated within 90 days of the filing of a report may result in costs for registered management investment companies. Many registered management investment companies may already regularly monitor and evaluate their procedures. However, the size and scope of these internal systems are likely to vary among registered management investment companies, and it is difficult to provide an accurate cost estimate.

Audit Committee Financial Experts

The added burden associated with the requirements to name the audit committee financial expert and disclose whether the audit committee financial expert is independent should be minimal. We have added a safe harbor provision to clarify that we do not intend to increase or decrease the current level of liability of audit committee members, or the audit committee member determined to be the expert, by requiring the disclosure as to whether an audit committee financial expert serves on the audit committee. We do not think that the requirement to name the audit committee financial expert should affect the expert's potential liability as an audit committee member. We requested comment on these costs, but received none.

Codes of Ethics

We also note that we are adopting rules that require a registered management investment company to provide disclosure of any codes of ethics applicable to its principal executive officer and senior financial officers, regardless of whether they are employees of the registrant or a third party and provide this disclosure on Form N–CSR or Form N–SAR (in the case of SBICs). This additional disclosure may impose certain costs such as retrieval, printing and copying costs. However, this information should be readily available to the board of directors and management of the investment company. Therefore, we estimate the additional costs to investment companies in complying with these provisions will be limited.

[107] *See* new rule 30a–3 under the Investment Company Act [17 CFR 270.30a–3].

We requested comment on these costs, but received none.

We note that we have modified our proposed rules to provide two alternatives to the code of ethics filing requirement. An investment company may either post its code of ethics on its website if it discloses that it intends to do so in its report on Form N–CSR or N–SAR, or undertake in its report on Form N–CSR or N–SAR to provide investors with a copy of its code of ethics upon request. These alternatives should allow registrants to choose the most cost-efficient method to meet the new requirements.

We believe that the additional audit committee financial expert and code of ethics requirements are necessary to implement the purposes of the Sarbanes-Oxley Act and will impose minimal additional burden on companies. For example, we expect that investment companies will incur added costs to disclose the name of the audit committee financial expert, to disclose whether that person is independent and to file or otherwise make available copies of their codes of ethics to investors. Investment companies electing to disclose their codes of ethics, and changes in and waivers from their codes of ethics, via their websites in lieu of publicly filing such disclosure on Form N–CSR or N–SAR must disclose this election in their reports on Form N–CSR or N–SAR. Such costs do not include the costs imposed on investment companies by the Sarbanes-Oxley Act itself. Rather, they reflect the costs of our requirements beyond the requirements of the Sarbanes-Oxley Act.

Total Cost Calculations

For purposes of the PRA,[108] with respect to Form N–SAR, we further estimate that the removal of the certification requirement will remove an incremental 41,010 hours from the current total burden hours or $6,151,500[109] and the disclosure of the code of ethics and audit committee financial experts will add an incremental 2 burden hours to the current total burden hours or $259.[110]

With respect to Form N–CSR, all respondents will incur an incremental increase of 35,139 burden hours[111] or $5,152,782[112] and $3,513,900 in outside legal costs[113] to comply with the amendments. The current total burden hours of Form 12b–25 will incrementally increase by 420 hours or $15,468[114] to comply with the amendments.

VI. Consideration of Burden on Competition; Promotion of Efficiency, Competition, and Capital Formation

Section 23(a)(2) of the Exchange Act requires us, when adopting rules under the Exchange Act, to consider the impact that any new rule would have on competition. Section 23(a)(2) also prohibits us from adopting any rule that would impose a burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act.[115] In addition, Section 2(c) of the Investment Company Act,[116] Section 2(b) of the Securities Act[117] and Section 3(f) of the Exchange Act[118] require the Commission, when engaging in rulemaking that requires it to consider or determine whether an action is necessary or appropriate in the public interest, to consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation. We received no comments relating to this specific section.

The new rules and rule and form amendments are intended to more fully implement the intent of Section 302 of the Sarbanes-Oxley Act that we adopt rules requiring the principal executive and financial officers of investment companies to certify the accuracy of their periodic reports filed pursuant to Section 13(a) or 15(d) of the Exchange Act. Also, the amendments are intended, in part, to increase transparency regarding the competence of the audit committee and the application of codes of ethics to a company's principal executive officer and senior financial officers. We believe that the amendments will benefit investors by providing them with greater confidence in the accuracy and completeness of the disclosure contained in the annual and semi-annual reports that they receive from management investment companies, including the financial statements. However, the magnitude of the effect of the amendments on efficiency, competition, and capital formation is difficult to quantify, particularly given that most management investment companies currently are required to comply with the certification requirements in recently adopted amendments to Form N–SAR, which we are removing as part of the amendments we are adopting today.

VII. Final Regulatory Flexibility Analysis

This Final Regulatory Flexibility Analysis (''Analysis'') has been prepared in accordance with 5 U.S.C. 604, and relates to the Commission's rules and rule and form amendments under the Exchange Act and the Investment Company Act that will require registered management investment companies to file certified shareholder reports on Form N–CSR with the Commission, will designate these certified reports as reports that are required under Sections 13(a) and 15(d) of the Exchange Act, and will implement Sections 406 and 407 of the Sarbanes-Oxley Act. Initial Regulatory Flexibility Analyses (''IRFAs''), which were prepared in accordance with 5 U.S.C. 603, were published in the release proposing Form N–CSR and in the release proposing rules to implement Sections 406 and 407 of the Sarbanes-Oxley Act.

The rule amendments require each registered management investment company's principal executive and financial officers to certify the information contained in these reports in the manner specified by Section 302

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[108] See Section IV above.

[109] 41,010 hours × $150 = $6,151,500. The estimate cost savings is derived from the estimated reduction in burden hours, and an estimated hourly wage rate for principal executive officers of $150.00. The hourly wage rates for principal executive and financial officers are not published. We arrived at $150.00 based on other hourly wage rates published and consultations with individuals who are familiar with the hourly wage rates. This wage rate includes 35% for overhead. *See* Securities Industry Association, *Report on Management & Professional Earnings in the Securities Industry 2001* (Oct. 2001).

[110] 2 hours × $129.81 = $259. The hourly wage rate of $129.81 is based on published hourly wage rates for the deputy general counsel. This wage rate includes 35% for overhead. *See* Securities Industry Association, *Report on Management & Professional Earnings in the Securities Industry 2001* (Oct. 2001).

[111] 43,150 hours for certification + 1,851 hours for audit committee financial expert disclosure + 1,851 hours for code of ethics disclosure = 46,852 hours × .75 = 35,139 hours.

[112] 35,139 hours × $146.64 = $5,152,782. This estimated wage rate of $146.64 is a blended rate, based on published hourly wage rates for a deputy general counsel outside of New York City ($129.81) and our estimated wage rate for principal executive and financial officers ($150.00). We estimate that principal executive and financial officers would spend 5 hours certifying the annual reports on Form N–CSR and a deputy general counsel would spend 1 hour completing the code of ethics and audit committee financial expert disclosures. This yields a weighted wage rate of $146.64 (($129.81 × 1/6) + ($150.00 × 5/6)) = $146.64. This weighted wage rate includes 35% for overhead. *See* Securities Industry Association, *Report on Management & Professional Earnings in the Securities Industry 2001* (Oct. 2001).

[113] 43,150 hours for certification + 1,851 hours for audit committee financial expert disclosure + 1,851 hours for code of ethics disclosure = 46,852 hours × .25 of outside counsel × $300 per hour = $3,513,900.

[114] 420 hours × $36.83 = $15,468. We estimate that an attorney with an hourly wage rate of $36.83 completes Form 12b–25. This wage rate includes 35% for overhead. *See* Securities Industry Association, *Report on Management & Professional Earnings in the Securities Industry 2001* (Oct. 2001).

[115] 15 U.S.C. 78w(a)(2).

[116] 15 U.S.C. 80a–2(c).

[117] 15 U.S.C. 77b(b).

[118] 15 U.S.C. 78c(f).

of the Sarbanes-Oxley Act of 2002. In addition, we are providing that, for registered management investment companies other than small business investment companies, Form N–SAR will be filed under the Investment Company Act of 1940 only and not the Securities Exchange Act of 1934. We are also removing the requirement that Form N–SAR be certified by a registered investment company's principal executive and financial officers. Furthermore, we are adopting a new rule to require every registered management investment company, other than small business investment companies, to maintain disclosure controls and procedures designed to ensure that the information required in reports on Form N–CSR is recorded, processed, summarized, and reported on a timely basis. Finally, we are requiring registered management investment companies to include new disclosures on Form N–CSR or Form N–SAR, as appropriate, in order to implement the requirements of Sections 406 and 407 of the Sarbanes-Oxley Act of 2002. First, the rules require a management investment company to disclose whether it has at least one ''audit committee financial expert'' serving on its audit committee, and if so, the name of the expert and whether the expert is independent of management. A management investment company that does not have an audit committee financial expert must disclose this fact and explain why it has no such expert. Second, the rules require a management investment company to disclose whether it has adopted a code of ethics that applies to the company's principal executive officer and senior financial officers, or persons performing similar functions, regardless of whether they are employed by the management investment company or a third party. A management investment company disclosing that it has not adopted such a code must disclose this fact and explain why it has not done so. A management investment company also will be required to disclose amendments to, and waivers from, the code of ethics relating to any of those officers.

A. Need for, and Objectives of, Amendments

The purpose of the new rules and rule and form amendments is to more fully implement the intent of Section 302 of the Sarbanes-Oxley Act that we adopt rules requiring the officers of investment companies to certify the accuracy of their periodic reports filed pursuant to Section 13(a) or 15(d) of the Exchange Act.

The amendments will require registered management investment companies to file with the Commission certified shareholder reports on Form N–CSR, and will designate these reports as filings which satisfy the reporting requirements of Sections 13(a) and 15(d) of the Exchange Act for management investment companies. We believe that by requiring the certification required by Section 302 of the Sarbanes-Oxley Act to be included in a management investment company's certified shareholder report on Form N–CSR, which contains financial statements, we are more fully implementing the intent of Section 302, which is to improve the quality of the disclosure that companies provide about their financial condition in their shareholder reports. In addition, we are adopting new disclosure requirements required to comply with Sections 406 and 407 of the Sarbanes-Oxley Act.

B. Significant Issues Raised by Public Comment

In both the IRFA for the release proposing Form N–CSR and the IRFA for the release proposing to implement Sections 406 and 407 of the Sarbanes-Oxley Act, we requested comment on any aspect of the IRFAs, including the number of small entities that would be affected by the proposal, the nature of the impact, how to quantify the numbers of small entities that would be affected, and how to quantify the impact of the proposals. We received one comment letter concerning the IRFA for the release proposing Form N–CSR. The commenter raised a concern that more flexible alternatives should have been considered for small investment companies (such as not mandating Form N–CSR or new reporting requirements at all) because a small amount of fraud is committed by such investment companies. We note that Congress' mandate for the Commission to require the certification specified by Section 302 of the Sarbanes-Oxley Act does not distinguish between small and large investment companies. Further, our disclosure rules generally do not distinguish between small and large investment companies. While we have the discretion to require that only larger investment companies file new Form N–CSR, it would not be appropriate to provide investors in larger investment companies with greater confidence in the accuracy and completeness of the disclosure contained in the annual and semi-annual reports that they receive from their investment companies, but not investors in small investment companies.

C. Small Entities Subject to the Rule

The new rules and rule and form amendments will affect registered investment companies that are small entities. For purposes of the Regulatory Flexibility Act (''RFA''), an investment company is a small entity if it, together with other investment companies in the same group of related investment companies, has net assets of $50 million or less as of the end of its most recent fiscal year.[119] We estimate that there are approximately 205 investment companies together with other investment companies in the same group of related investment companies that have net assets of $50 million or less as of the end of its most recent fiscal year.[120]

D. Reporting, Recordkeeping, and Other Compliance Requirements

The new rules and rule and form amendments will require management investment companies to file certified shareholder reports on Form N–CSR, containing (i) a copy of any required shareholder report, (ii) additional information regarding disclosure controls and procedures, and (iii) the certification required by Section 302 of the Sarbanes-Oxley Act. The form of the certification will parallel the form of the certification we adopted on Form N–SAR, and on Forms 10–K and 10–Q. The certification will require the management investment company's principal executive and financial officers to state, in part, that, based on their knowledge, the information in the certified shareholder report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made not misleading with respect to the period covered by the report, and that the financial statements, and other financial information included in the report, fairly present the financial condition, results of operations, changes in net assets, and cash flows (if the financial statements are required to include a statement of cash flows) of the registrant. The certification also will require the signing officers to certify that they have established and maintained disclosure controls and procedures to ensure that material

[119] 17 CFR 270.0–10.

[120] This estimate is based on figures compiled by the Commission staff regarding investment companies registered on Form N–1A, Form N–2, and Form N–3. In determining whether an insurance company separate account is a small entity for purposes of the Regulatory Flexibility Act, the assets of insurance company separate accounts are aggregated with the assets of their sponsoring insurance companies. Investment Company Act rule 0–10(b) [17 CFR 270.0–10(b)].

information relating to the registrant is made known to senior management, and also to certify that they have evaluated these procedures within 90 days of the filing date of the report. The amendments may increase the costs associated with compliance with investment companies' reporting obligations. However, this cost increase is expected to be limited, because most management investment companies are currently required to provide a similar certification with respect to their reports on Form N–SAR.

In addition, the amendments will require registered management investment companies to disclose information regarding whether an audit committee financial expert serves on the investment company's audit committee and whether the investment company has adopted a code of ethics that applies to the investment company's principal executive officer and senior financial officers. All registered management investment companies, including those that are not required to file reports pursuant to Section 13(a) or 15(d) of the Exchange Act, will be subject to these amendments. Because the disclosure requirements of these amendments will be new, management investment companies may need to hire outside counsel or other third parties to prepare the new disclosure. We expect that reporting information in response to these new disclosure items will increase costs incurred by small entities because the new disclosure items will require these entities to compile and report more information. For purposes of the PRA and our cost-benefit analysis,[121] with respect to Form N–SAR, we further estimate that the removal of the certification requirement will remove an incremental 41,010 hours from the current total burden hours, equivalent to a cost of $6,151,500§ [122] and the disclosure of the code of ethics and audit committee financial experts will add an incremental 2 burden hours to the current total burden hours, equivalent to a cost of $259.[123] With respect to Form N–CSR, all respondents will incur an incremental increase of 35,139 burden hours,[124] equivalent to internal costs of $5,152,782§ [125] and $3,513,900 in outside legal costs [126] to comply with the amendments. The current total burden hours of Form 12b-25 will incrementally increase by 420 hours or $15,468 [127] as a result of the amendments.

E. Agency Action to Minimize Effect on Small Entities

As required by Section 603 of the RFA, and with respect to Sections 302, 406, and 407 of the Sarbanes-Oxley Act, the Commission has considered the following alternatives to minimize the economic impact of the proposed rules and rule amendments on small entities: (i) The establishment of differing compliance or reporting requirements that take into account the resources available to small entities; (ii) the clarification, consolidation, or simplification of compliance and reporting requirements under the proposed amendments for small entities; and (iii) an exemption from coverage of the proposed amendments, or any part thereof, for small entities.

The rules we are adopting are intended to more fully implement the intent of Section 302 of the Sarbanes-Oxley Act, and should help ensure that information about an investment company's business and financial condition, specifically its financial statements, is adequately reviewed by an investment company's senior executives, thereby enhancing investor confidence in the quality of its disclosure. In addition, the rules we are adopting implement Sections 406 and 407 of the Sarbanes-Oxley Act by requiring disclosure with respect to codes of ethics and audit committee financial experts to provide investors better understanding of the ethical principles and background and affiliations of the executives and directors of the investment company.

The Commission believes at the present time that special compliance or reporting requirements for small entities, or an exemption from coverage for small entities, would not be appropriate or consistent with investor protection. The designation of certified shareholder reports on Form N–CSR as reporting forms that must contain the certification required by Section 302 of the Sarbanes-Oxley Act is intended to improve investor confidence in the quality of an investment company's disclosure to investors in its shareholder reports, particularly the financial statements contained in these reports. We believe it is important that the benefits resulting from the certification of shareholder reports as required by the new rules be provided to investors in all management investment companies, not just investors in management investment companies that are not considered small entities. The Commission also notes that Section 302 of the Sarbanes-Oxley Act does not distinguish between small entities and other investment companies. Similarly, Sections 406 and 407 of the Sarbanes-Oxley Act do not distinguish between small entities and other investment companies.

We believe that different compliance or reporting requirements or timetables for small entities would interfere with achieving the primary goal of increasing transparency of corporate activities and internal procedures. We generally believe that an exemption for small entities from coverage of the new rules is not appropriate and is inconsistent with the policies underlying the Sarbanes-Oxley Act. We also think that the disclosure requirements relating to the audit committee financial experts and codes of ethics are clear and straightforward. In addition, we are not aware of any way to clarify or simplify compliance for small entities.

VIII. Statutory Authority

The rules and rule and form amendments contained in this release are being adopted pursuant to Sections 10(b), 13, 15(d), 23(a), and 36 of the Exchange Act [15 U.S.C. 78j(b), 78m, 78o(d), 78w(a), and 78mm], Sections 6(c), 8, 24(a), 30, and 38 of the Investment Company Act [15 U.S.C. 80a–6(c), 80a–8, 80a–24(a), 80a–29, and 80a–37], and Sections 3(a), 302, 406, and 407 of the Sarbanes–Oxley Act of 2002 [Pub. L. 107–204, 116 Stat. 745].

List of Subjects

17 CFR Parts 240 and 249

Reporting and recordkeeping requirements, Securities.

17 CFR Parts 270 and 274

Investment companies, Reporting and recordkeeping requirements, Securities.

Text of Amendments

In accordance with the foregoing, Title 17, Chapter II, of the Code of Federal Regulations is amended as follows:

[121] *See* Sections IV and V above.

[122] 41,010 hours × $150 = $6,151,500. *See supra* note 109 (explaining the wage rate).

[123] 2 hours × $129.81 = $259. *See supra* note (explaining the wage rate).

[124] 43,150 hours for certification + 1,851 hours for audit committee financial expert disclosure + 1,851 hours for code of ethics disclosure = 46,852 hours × .75 = 35,139 hours.

[125] 35,139 hours × $146.64 = $5,152,782. *See supra* note 112 (explaining the wage rate).

[126] 43,150 hours for certification + 1,851 hours for audit committee financial expert disclosure + 1,851 hours for code of ethics disclosure = 46,852 hours × .25 of outside counsel × $300 per hour = $3,513,900.

[127] 420 hours × $36.83 = $15,468. *See supra* note 114 (explaining the wage rate).

PART 240—GENERAL RULES AND REGULATIONS, SECURITIES EXCHANGE ACT OF 1934

1. The authority citation for Part 240 is amended by adding the specific authority for ''Section 240.12b–25'' in numerical order to read as follows:

Authority: 15 U.S.C. 77c, 77d, 77g, 77j, 77s, 77z–2, 77z–3, 77eee, 77ggg, 77nnn, 77sss, 77ttt, 78c, 78d, 78e, 78f, 78g, 78i, 78j, 78j–1, 78k, 78k–1, 78*l*, 78m, 78n, 78o, 78p, 78q, 78s, 78u–5, 78w, 78x, 78*ll*, 78mm, 79q, 79t, 80a–20, 80a–23, 80a–29, 80a–37, 80b–3, 80b–4 and 80b–11, unless otherwise noted.

* * * * *

Section 240.12b–25 is also issued under 15 U.S.C. 80a–8, 80a–24(a), 80a–29, and 80a–37.

* * * * *

2. Section 240.12b–25 is amended by revising the section heading and paragraphs (a) and (b)(2)(ii) to read as follows:

§ 240.12b–25 Notification of inability to timely file all or any required portion of a Form 10–K, 10–KSB, 20–F, 11–K, N–SAR, N–CSR, 10–Q or 10–QSB.

(a) If all or any required portion of an annual or transition report on Form 10–K, 10–KSB, 20–F or 11–K (17 CFR 249.310, 249.310b, 249.220f or 249.311), or a quarterly or transition report on Form 10–Q or 10–QSB (17 CFR 249.308a or 249.308b) required to be filed pursuant to sections 13 or 15(d) of the Act (15 U.S.C. 78m or 78o(d)) and rules thereunder, or if all or any required portion of a semi-annual, annual or transition report on Form N–CSR (17 CFR 249.331; 17 CFR 274.128) or Form N–SAR (17 CFR 249.330; 17 CFR 274.101) required to be filed pursuant to sections 13 or 15(d) of the Act or section 30 of the Investment Company Act of 1940 (15 U.S.C. 80a–29) and the rules thereunder, is not filed within the time period prescribed for such report, the registrant, no later than one business day after the due date for such report, shall file a Form 12b–25 (17 CFR 249.322) with the Commission which shall contain disclosure of its inability to file the report timely and the reasons therefor in reasonable detail.

(b) * * *

(2) * * *

(ii) The subject annual report, semi-annual report or transition report on Form 10–K, 10–KSB, 20–F, 11–K, N–SAR, or N–CSR, or portion thereof, will be filed no later than the fifteenth calendar day following the prescribed due date; or the subject quarterly report or transition report on Form 10–Q or 10–QSB, or portion thereof, will be filed no later than the fifth calendar day following the prescribed due date; and

* * * * *

3. Section 240.13a–15 is amended by revising paragraph (a) to read as follows:

§ 240.13a–15 Issuer's disclosure controls and procedures related to preparation of required reports.

(a) Every issuer that has a class of securities registered pursuant to section 12 of the Act (15 U.S.C. 78*l*), other than an Asset-Backed Issuer (as defined in § 240.13a–14(g) of this chapter), a small business investment company registered on Form N–5 (§§ 239.24 and 274.5 of this chapter), or a unit investment trust as defined by Section 4(2) of the Investment Company Act of 1940 (15 U.S.C. 80a–4(2)), must maintain disclosure controls and procedures (as defined in § 240.13a–14(c) of this chapter).

* * * * *

4. Section 240.15d–15 is amended by revising paragraph (a) to read as follows:

§ 240.15d–15 Issuer's disclosure controls and procedures related to preparation of required reports.

(a) Every issuer that files reports under section 15(d) of the Act (15 U.S.C. 78o(d)), other than an Asset-Backed Issuer (as defined in § 240.13a–14(g) of this chapter), a small business investment company registered on Form N–5 (§§ 239.24 and 274.5 of this chapter), or a unit investment trust as defined by Section 4(2) of the Investment Company Act of 1940 (15 U.S.C. 80a–4(2)), must maintain disclosure controls and procedures (as defined in § 240.15d–14(c) of this chapter).

* * * * *

PART 249—FORMS, SECURITIES EXCHANGE ACT OF 1934

5. The authority citation for Part 249 is amended by adding the following citations in numerical order to read as follows:

Authority: 15 U.S.C. 78a, *et seq.*, unless otherwise noted.

* * * * *

Section 249.330 is also issued under secs. 3(a), 406, and 407, Pub. L. No. 107–204, 116 Stat. 745.

Section 249.331 is also issued under secs. 3(a), 302, 406, and 407, Pub. L. 107–204, 116 Stat. 745.

6. Section 249.322 is amended by revising paragraph (a) to read as follows:

§ 249.322 Form 12b–25—Notification of late filing.

(a) This form shall be filed pursuant to § 240.12b–25 of this chapter by issuers who are unable to file timely all or any required portion of an annual or transition report on Form 10–K and Form 10–KSB, 20–F, or 11–K (§§ 249.310, 249.310b, 249.220f or 249.311) or a quarterly or transition report on Form 10–Q and Form 10–QSB (§§ 249.308a and 249.308b) pursuant to section 13 or 15(d) of the Act (15 U.S.C. 78m or 78o(d)) or a semi-annual, annual, or transition report on Form N–SAR (§§ 249.330; 274.101) or Form N–CSR (§§ 249.331; 274.128) pursuant to section 13 or 15(d) of the Act or section 30 of the Investment Company Act of 1940 (15 U.S.C. 80a–29). The filing shall consist of a signed original and three conformed copies, and shall be filed with the Commission at Washington, DC 20549, no later than one business day after the due date for the periodic report in question. Copies of this form may be obtained from ''Publications,'' Securities and Exchange Commission, 450 5th Street, NW., Washington, DC 20549 and at our Web site at *http://www.sec.gov.*

* * * * *

7. Form 12b–25 (referenced in § 249.322) is amended by:

a. Revising the preamble;

b. Revising paragraph (b) of Part II; and

c. Revising Part III to read as follows:

Note: The text of Form 12b–25 does not, and this amendment will not, appear in the Code of Federal Regulations.

Form 12b–25

Notification of Late Filing

(Check One): __ Form 10–K __ Form 20–F __ Form 11–K __ Form 10–Q __ Form N–SAR __ Form N–CSR

* * * * *

Part II—Rules 12b–25(b) and (c)

* * * * *

(b) The subject annual report, semi-annual report, transition report on Form 10–K, Form 20–F, Form 11–K, Form N–SAR or Form N–CSR, or portion thereof, will be filed on or before the fifteenth calendar day following the prescribed due date; or the subject quarterly report or transition report on Form 10–Q, or portion thereof, will be filed on or before the fifth calendar day following the prescribed due date; and

* * * * *

Part III—Narrative

State below in reasonable detail why Forms 10–K, 20–F, 11–K, 10–Q, N–SAR, N–CSR, or the transition report or portion thereof, could not be filed within the prescribed time period.

* * * * *

8. Section 249.330 is revised to read as follows:

§ 249.330 Form N–SAR, annual and semi-annual report of certain registered investment companies.

This form shall be used by registered unit investment trusts and small business investment companies for semi-annual or annual reports to be filed pursuant to § 270.30a–1 or § 270.30b1–1 of this chapter in satisfaction of the requirement of section 30(a) of the Investment Company Act of 1940 that every registered investment company must file annually with the Commission such information, documents, and reports as investment companies having securities registered on a national securities exchange are required to file annually pursuant to section 13(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78m) and the rules and regulations thereunder.

9. Section 249.331 is added to read as follows:

§ 249.331 Form N–CSR, certified shareholder report.

This form shall be used by registered management investment companies to file reports pursuant to § 270.30b2–1(a) of this chapter not later than 10 days after the transmission to stockholders of any report that is required to be transmitted to stockholders under § 270.30e–1 of this chapter.

PART 270—RULES AND REGULATIONS, INVESTMENT COMPANY ACT OF 1940

10. The authority citation for Part 270 is amended by revising the general authority citation and the specific authority for ''Section 270.30a–2'' and adding the following citations in numerical order to read as follows:

Authority: 15 U.S.C. 80a–1 *et seq.*, 80a–34(d), 80a–37, and 80a–39, unless otherwise noted.

* * * * *

Section 270.30a–1 is also issued under 15 U.S.C. 78m, 78o(d), 80a–8, and 80a–29.

Section 270.30a–2 is also issued under 15 U.S.C. 78m, 78o(d), 80a–8, and 80a–29, and secs. 3(a) and 302, Pub. L. 107–204, 116 Stat. 745.

Section 270.30a–3 is also issued under 15 U.S.C. 78m, 78o(d), 80a–8, and 80a–29, and secs. 3(a) and 302, Pub. L. 107–204, 116 Stat. 745.

Section 270.30b1–1 is also issued under 15 U.S.C. 78m, 78o(d), 80a–8, and 80a–29.

Section 270.30b2–1 is also issued under 15 U.S.C. 78m, 78o(d), 80a–8, and 80a–29, and secs. 3(a) and 302, Pub. L. 107–204, 116 Stat. 745.

Section 270.30d–1 is also issued under 15 U.S.C. 78m, 78o(d), 80a–8, and 80a–29, and secs. 3(a) and 302, Pub. L. 107–204, 116 Stat. 745.

* * * * *

11. Section 270.8b–15 is amended by adding a sentence at the end of the section to read as follows:

§ 270.8b–15 Amendments.

* * * An amendment to any report required to include the certification as specified in § 270.30a–2 must provide a new certification by each principal executive officer and principal financial officer of the registrant.

12. Section 270.30a–1 is revised to read as follows:

§ 270.30a–1 Annual reports for unit investment trusts.

Every registered unit investment trust shall file an annual report on Form N–SAR with respect to each calendar year not more than sixty calendar days after the close of each year. A registered unit investment trust that has filed a registration statement with the Commission registering its securities for the first time under the Securities Act of 1933 is relieved of this reporting obligation with respect to any reporting period or portion thereof prior to the date on which that registration statement becomes effective or is withdrawn.

13. Section 270.30a–2 is revised by:

a. Revising the section heading; and

b. Revising paragraphs (a) and (c) to read as follows:

§ 270.30a–2 Certification of Form N–CSR.

(a) Each report filed on Form N–CSR (§§ 249.331 and 274.128 of this chapter) by a registered management investment company must include a certification containing the information set forth in paragraph (b) of this section in the form specified in the report. Each principal executive officer or officers and principal financial officer or officers of the investment company, or persons performing similar functions, at the time of filing of the report must sign the certification.

* * * * *

(c) For purposes of this section and § 270.30a–3, the term ''disclosure controls and procedures'' means controls and other procedures of a registered management investment company that are designed to ensure that information required to be disclosed by the investment company on Form N–CSR is recorded, processed, summarized, and reported within the time periods specified in the Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an investment company in the reports that it files or submits on Form N–CSR is accumulated and communicated to the investment company's management, including its principal executive officer or officers and principal financial officer or officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

* * * * *

14. Section 270.30a–3 is added to read as follows:

§ 270.30a–3 Disclosure controls and procedures related to preparation of required filings.

(a) Every registered management investment company, other than a small business investment company registered on Form N–5 (§§ 239.24 and 274.5 of this chapter), must maintain disclosure controls and procedures (as defined in § 270.30a–2(c)).

(b) Within the 90-day period prior to the filing date of each report requiring certification under § 270.30a–2, an evaluation must be carried out under the supervision, and with the participation of, the registered management investment company's management, including the registered management investment company's principal executive officer or officers and principal financial officer or officers, or persons performing similar functions, of the effectiveness of the design and operation of the registered management investment company's disclosure controls and procedures.

15. Section 270.30b1–1 is revised to read as follows:

§ 270.30b1–1 Semi-annual report for registered management investment companies.

Every registered management investment company shall file a semi-annual report on Form N–SAR (§ 274.101 of this chapter) not more than sixty calendar days after the close of each fiscal year and fiscal second quarter. A registered management investment company that has filed a registration statement with the Commission registering its securities for the first time under the Securities Act of 1933 is relieved of this reporting obligation with respect to any reporting period or portion thereof prior to the date on which that registration statement becomes effective or is withdrawn.

16. Section 270.30b1–3 is revised to read as follows:

§ 270.30b1–3 Transition reports.

Every registered management investment company filing reports on Form N–SAR that changes its fiscal year end shall file a report on Form N–SAR not more than 60 calendar days after the later of either the close of the transition period or the date of the determination to change the fiscal year end which report shall not cover a period longer than six months.

17. Section 270.30b2–1 is revised to read as follows:

§ 270.30b2–1 Filing of reports to stockholders.

(a) Every registered management investment company shall file a report on Form N–CSR (§§ 249.331 and 274.128 of this chapter) not later than 10 days after the transmission to stockholders of any report that is required to be transmitted to stockholders under § 270.30e–1.

(b) A registered investment company shall file with the Commission a copy of every periodic or interim report or similar communication containing financial statements that is transmitted by or on behalf of such registered investment company to any class of such company's security holders and that is not required to be filed with the Commission under paragraph (a) of this section. The filing shall be made not later than 10 days after the transmission to security holders.

18. Section 270.30d–1 is added to read as follows:

§ 270.30d–1 Designation of periodic reports under the Securities Exchange Act of 1934.

A registered management investment company, other than a small business investment company registered on Form N–5 (§§ 239.24 and 274.5 of this chapter), that is required to file annual and quarterly reports pursuant to section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m(a) or 78o(d)) shall satisfy its requirement to file such reports by the filing, in accordance with the rules and procedures specified therefor, of reports on Form N–CSR (§§ 249.331 and 274.128 of this chapter). A registered unit investment trust or a small business investment company registered on Form N–5 that is required to file annual and quarterly reports pursuant to section 13(a) or 15(d) of the Securities Exchange Act of 1934 shall satisfy its requirement to file such reports by the filing, in accordance with the rules and procedures specified therefor, of reports on Form N–SAR (§§ 249.330 and 274.101 of this chapter).

PART 274—FORMS PRESCRIBED UNDER THE INVESTMENT COMPANY ACT OF 1940

19. The authority citation for Part 274 is revised to read as follows:

Authority: 15 U.S.C. 77f, 77g, 77h, 77j, 77s, 78c(b), 78l, 78m, 78n, 78o(d), 80a–8, 80a–24, 80a–26, and 80a–29, unless otherwise noted.

Section 274.101 is also issued under secs. 3(a), 406, and 407, Pub. L. 107–204, 116 Stat. 745.

Section 274.128 is also issued under secs. 3(a), 302, 406, and 407, Pub. L. 107–204, 116 Stat. 745.

20. Section 274.101 is revised to read as follows:

§ 274.101 Form N–SAR, semi-annual report of registered investment companies.

This form shall be used by registered management investment companies for semi-annual or annual reports to be filed pursuant to rule 30b1–1 (17 CFR 270.30b1–1) and by registered unit investment trusts for annual reports to be filed pursuant to rule 30a–1 (17 CFR 270.30a–1).

21. Form N–SAR (referenced in §§ 249.330 and 274.101) is amended by:

a. Revising the reference ''133'' in item 6 to read ''132'';

b. Removing item 133;

c. Revising the first, fifth, and sixth paragraphs of General Instruction A;

d. Removing the reference ''and item 133'' at the end of paragraph (1) of General Instruction D;

e. Removing paragraph (5) of General Instruction G;

f. Revising the Instruction to sub-item 77Q3 in Instructions to Specific Items;

g. Revising the Instruction to sub-item 102P3 in Instructions to Specific Items;

h. Removing the Instruction to Item 133 in Instructions to Specific Items; and

i. Revising the reference ''133'' in the Signature Page section in Instructions to Specific Items to read ''132''.

These additions and revisions read as follows:

Note: The text of Form N–SAR does not, and this amendment will not, appear in the Code of Federal Regulations.

Form N–SAR

* * * * *

General Instructions

A. Rule as to Use of Form N–SAR

Form N–SAR is a reporting form that is to be used for semi-annual and annual reports by all registered investment companies that have filed a registration statement which has become effective pursuant to the Securities Act of 1933 (''1933 Act'') with the exception of face amount certificate companies. Face amount certificate companies should continue to file periodic reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 (''1934 Act''). Registered management investment companies, other than small business investment companies, are required to file semi-annual and annual reports on Form N–SAR under the Investment Company Act of 1940 (the ''Act'') and rule 30b1–1 (17 CFR 270.30b1–1) under the Act. Registered small business investment companies are required to file semi-annual and annual reports under the Act and rule 30b1–1 (17 CFR 270.30b1–1) under the Act, and, if applicable, Section 13 or 15(d) of the 1934 Act. Registered unit investment trusts (''UITs'') are required to file annual reports on Form N–SAR under the Act and rule 30a–1 (17 CFR 270.30a–1) under the Act, and, if applicable, Section 13 or 15(d) of the 1934 Act.

* * * * *

Unit investment trusts: The fourth section of the form, which contains items 111 through 132, is to be completed only by all UITs. Each UIT is required to complete appropriate items in this section once a year for the 12-month period ending December 31 and to include information for all of its series.

Under Section 30 of the Act, Sections 13 and 15(d) of the 1934 Act, and the rules and regulations thereunder, the Commission is authorized to solicit the information required by Form N–SAR from registered investment companies. Disclosure of the information specified on Form N–SAR is mandatory. Information supplied on Form N–SAR will be included routinely in the public files of the Commission and will be available for inspection by any interested persons.

* * * * *

Instructions to Specific Items

* * * * *

Sub-Item 77Q3

Furnish any other information required to be included as an exhibit pursuant to such rules and regulations as the Commission may prescribe.

* * * * *

Sub-Item 102P3

(a)(1)Disclose whether, as of the end of the period covered by the report, the registrant has adopted a code of ethics that applies to the registrant's principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing

similar functions, regardless of whether these individuals are employed by the registrant or a third party. If the registrant has not adopted such a code of ethics, explain why it has not done so. The information required by this paragraph (a)(1) is only required in an annual report on this Form N–SAR.

(2) For purposes of this Instruction 102P3(a), the term ''code of ethics'' means written standards that are reasonably designed to deter wrongdoing and to promote:

(i) Honest and ethical conduct, including the ethical handling of actual or apparent conflicts of interest between personal and professional relationships;

(ii) Full, fair, accurate, timely, and understandable disclosure in reports and documents that a registrant files with, or submits to, the Commission and in other public communications made by the registrant;

(iii) Compliance with applicable governmental laws, rules, and regulations;

(iv) The prompt internal reporting of violations of the code to an appropriate person or persons identified in the code; and

(v) Accountability for adherence to the code.

(3) The registrant must briefly describe the nature of any amendment, during the period covered by the report, to a provision of its code of ethics that applies to the registrant's principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions, regardless of whether these individuals are employed by the registrant or a third party, and that relates to any element of the code of ethics definition enumerated in paragraph (a)(2) of this Instruction 102P3. The registrant must file a copy of any such amendment as an exhibit to this report on Form N–SAR, unless the registrant has elected to satisfy paragraph (a)(6) of this Instruction 102P3 by posting its code of ethics on its website pursuant to paragraph (a)(6)(ii) of this Instruction 102P3, or by undertaking to provide its code of ethics to any person without charge, upon request, pursuant to paragraph (a)(6)(iii) of this Instruction 102P3.

(4) If the registrant has, during the period covered by the report, granted a waiver, including an implicit waiver, from a provision of the code of ethics to the registrant's principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions, regardless of whether these individuals are employed by the registrant or a third party, that relates to one or more of the items set forth in paragraph (a)(2) of this Instruction 102P3, the registrant must briefly describe the nature of the waiver, the name of the person to whom the waiver was granted, and the date of the waiver.

(5) If the registrant intends to satisfy the disclosure requirement under paragraph (a)(3) or (4) of this Instruction 102P3 regarding an amendment to, or a waiver from, a provision of its code of ethics that applies to the registrant's principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions and that relates to any element of the code of ethics definition enumerated in paragraph (a)(2) of this Instruction 102P3 by posting such information on its Internet website, disclose the registrant's Internet address and such intention.

(6) The registrant must:

(i) File with the Commission a copy of its code of ethics that applies to the registrant's principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions, as an exhibit to its annual report on this Form N–SAR;

(ii) Post the text of such code of ethics on its Internet website and disclose, in its most recent report on this Form N–SAR, its Internet address and the fact that it has posted such code of ethics on its Internet website; or

(iii) Undertake in its most recent report on this Form N–SAR to provide to any person without charge, upon request, a copy of such code of ethics and explain the manner in which such request may be made.

(7) A registrant may have separate codes of ethics for different types of officers. Furthermore, a ''code of ethics'' within the meaning of paragraph (a)(2) of this Instruction 102P3 may be a portion of a broader document that addresses additional topics or that applies to more persons than those specified in paragraph (a)(1). In satisfying the requirements of paragraph (a)(6), a registrant need only file, post, or provide the portions of a broader document that constitutes a ''code of ethics'' as defined in paragraph (a)(2) and that apply to the persons specified in paragraph (a)(1).

(8) If a registrant elects to satisfy paragraph (a)(6) of this Instruction 102P3 by posting its code of ethics on its website pursuant to paragraph (a)(6)(ii), the code of ethics must remain accessible on its website for as long as the registrant remains subject to the requirements of this Instruction 102P3 and chooses to comply with this Instruction 102P3 by posting its code on its website pursuant to paragraph (a)(6)(ii).

(9) The registrant does not need to provide any information pursuant to paragraphs (a)(3) and (4) of this Instruction 102P3 if it discloses the required information on its Internet website within five business days following the date of the amendment or waiver and the registrant has disclosed in its most recently filed report on this Form N–SAR its Internet address and intention to provide disclosure in this manner. If the amendment or waiver occurs on a Saturday, Sunday, or holiday on which the Commission is not open for business, then the five business day period shall begin to run on and include the first business day thereafter. If the registrant elects to disclose this information through its website, such information must remain available on the website for at least a 12-month period. The registrant must retain the information for a period of not less than six years following the end of the fiscal year in which the amendment or waiver occurred. Upon request, the registrant must furnish to the Commission or its staff a copy of any or all information retained pursuant to this requirement.

(10) The registrant does not need to disclose technical, administrative, or other non-substantive amendments to its code of ethics.

(11) For purposes of this Instruction 102P3(a):

(i) The term ''waiver'' means the approval by the registrant of a material departure from a provision of the code of ethics; and

(ii) The term ''implicit waiver'' means the registrant's failure to take action within a reasonable period of time regarding a material departure from a provision of the code of ethics that has been made known to an executive officer, as defined in rule 3b–7 under the 1934 Act (17 CFR 240.3b–7), of the registrant.

(b)(1) Disclose that the registrant's board of directors has determined that the registrant either:

(i) Has at least one audit committee financial expert serving on its audit committee; or

(ii) Does not have an audit committee financial expert serving on its audit committee.

(2) If the registrant provides the disclosure required by paragraph (b)(1)(i) of this Instruction 102P3, it must disclose the name of the audit committee financial expert and whether that person is ''independent.'' In order to be considered ''independent'' for purposes of this Instruction 102P3(b), a member of an audit committee may not,

other than in his or her capacity as a member of the audit committee, the board of directors, or any other board committee:

(i) Accept directly or indirectly any consulting, advisory, or other compensatory fee from the issuer; or

(ii) Be an ''interested person'' of the investment company as defined in Section 2(a)(19) of the Act (15 U.S.C. 80a–2(a)(19)).

(3) If the registrant provides the disclosure required by paragraph (b)(1)(ii) of this Instruction 102P3, it must explain why it does not have an audit committee financial expert.

(4) The information required by paragraphs (b)(1) ''–(3) of this Instruction 102P3 is only required in an annual report on Form N–SAR.

(5) If the registrant's board of directors has determined that the registrant has more than one audit committee financial expert serving on its audit committee, the registrant may, but is not required to, disclose the names of those additional persons. A registrant choosing to identify such persons must indicate whether they are independent pursuant to paragraph (b)(2) of this Instruction 102P3.

(6) For purposes of this Instruction 102P3, an ''audit committee financial expert'' means a person who has the following attributes:

(i) An understanding of generally accepted accounting principles and financial statements;

(ii) The ability to assess the general application of such principles in connection with the accounting for estimates, accruals, and reserves;

(iii) Experience preparing, auditing, analyzing, or evaluating financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of issues that can reasonably be expected to be raised by the registrant's financial statements, or experience actively supervising one or more persons engaged in such activities;

(iv) An understanding of internal controls and procedures for financial reporting; and

(v) An understanding of audit committee functions.

(7) A person shall have acquired such attributes through:

(i) Education and experience as a principal financial officer, principal accounting officer, controller, public accountant, or auditor or experience in one or more positions that involve the performance of similar functions;

(ii) Experience actively supervising a principal financial officer, principal accounting officer, controller, public accountant, auditor, or person performing similar functions;

(iii) Experience overseeing or assessing the performance of companies or public accountants with respect to the preparation, auditing, or evaluation of financial statements; or

(iv) Other relevant experience.

(8)(i) A person who is determined to be an audit committee financial expert will not be deemed an ''expert'' for any purpose, including without limitation for purposes of Section 11 of the 1933 Act (15 U.S.C. 77k), as a result of being designated or identified as an audit committee financial expert pursuant to this Instruction 102P3(b).

(ii) The designation or identification of a person as an audit committee financial expert pursuant to this Instruction 102P3(b) does not impose on such person any duties, obligations, or liability that are greater than the duties, obligations, and liability imposed on such person as a member of the audit committee and board of directors in the absence of such designation or identification.

(iii) The designation or identification of a person as an audit committee financial expert pursuant to this Instruction 102P3(b) does not affect the duties, obligations, or liability of any other member of the audit committee or board of directors.

(9) If a person qualifies as an audit committee financial expert by means of having held a position described in paragraph (b)(7)(iv) of this Instruction 102P3, the registrant shall provide a brief listing of that person's relevant experience.

(c) Furnish any other information required to be included as an exhibit pursuant to such rules and regulations as the Commission may prescribe.

* * * * *

22. Section 274.128 and Form N–CSR (referenced in §§ 249.331 and 274.128) are added to read as follows:

§ 274.128 Form N–CSR, certified shareholder report.

This form shall be used by registered management investment companies to file reports pursuant to § 270.30b2–1(a) of this chapter not later than 10 days after the transmission to stockholders of any report that is required to be transmitted to stockholders under § 270.30e–1 of this chapter.

* * * * *

Note: The text of Form N–CSR does not, and this amendment will not, appear in the *Code of Federal Regulations.*

FORM N–CSR

Certified Shareholder Report of Registered Management Investment Companies

Investment Company Act file number __

_____

(Exact name of registrant as specified in charter)

_____

(Address of principal executive offices) (Zip code)

_____

(Name and address of agent for service)

Registrant's telephone number, including area code: _____

Date of fiscal year end: _____

Date of reporting period: _____

Form N–CSR is to be used by management investment companies to file reports with the Commission not later than 10 days after the transmission to stockholders of any report that is required to be transmitted to stockholders under Rule 30e–1 under the Investment Company Act of 1940 (17 CFR 270.30e–1). The Commission may use the information provided on Form N–CSR in its regulatory, disclosure review, inspection, and policymaking roles.

A registrant is required to disclose the information specified by Form N–CSR, and the Commission will make this information public. A registrant is not required to respond to the collection of information contained in Form N–CSR unless the Form displays a currently valid Office of Management and Budget (''OMB'') control number. Please direct comments concerning the accuracy of the information collection burden estimate and any suggestions for reducing the burden to Secretary, Securities and Exchange Commission, 450 Fifth Street, NW, Washington, DC 20549–0609. The OMB has reviewed this collection of information under the clearance requirements of 44 U.S.C. 3507.

General Instructions

A. Rule as to Use of Form N–CSR

Form N–CSR is a combined reporting form that is to be used for reports of registered management investment companies under Section 30(b)(2) of the Investment Company Act of 1940 (the ''Act'') and Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (the ''Exchange Act''), filed pursuant to Rule 30b2–1(a) under the Act (17 CFR 270.30b2–1(a)). A report on this Form shall be filed within 10 days after the transmission to stockholders of any annual or semi-annual report that is required to be transmitted to

stockholders pursuant to Rule 30e–1 under the Act (17 CFR 270.30e–1).

B. Application of General Rules and Regulations

The General Rules and Regulations under the Act and the Exchange Act contain certain general requirements that are applicable to reporting on any form under those Acts. These general requirements should be carefully read and observed in the preparation and filing of reports on this form, except that any provision in the form or in these instructions shall be controlling.

C. Preparation of Report

1. This Form is not to be used as a blank form to be filled in, but only as a guide in preparing the report in accordance with Rules 8b–11 (17 CFR 270.8b–11) and 8b–12 (17 CFR 270.8b–12) under the Act and Rules 12b–11 (17 CFR 240.12b–11) and 12b–12 (17 CFR 240.12b–12) under the Exchange Act. The Commission does not furnish blank copies of this Form to be filled in for filing.

2. These general instructions are not to be filed with the report.

3. Attention is directed to Rule 12b–20 under the Exchange Act (17 CFR 240.12b–20), which states: ''In addition to the information expressly required to be included in a statement or report, there shall be added such further material information, if any, as may be necessary to make the required statements, in the light of the circumstances under which they are made not misleading.''

D. Incorporation by Reference

A registrant may incorporate by reference information required by Item 10(a), but no other Items of the Form shall be answered by incorporating any information by reference. All incorporation by reference must comply with the requirements of this Form and the following rules on incorporation by reference: Rule 10(d) of Regulation S–K under the Securities Act of 1933 (17 CFR 229.10(d)) (general rules on incorporation by reference, which, among other things, prohibit, unless specifically required by this Form, incorporating by reference a document that includes incorporation by reference to another document, and limits incorporation to documents filed within the last 5 years, with certain exceptions); Rule 303 of Regulation S–T (17 CFR 232.303) (specific requirements for electronically filed documents); Rules 12b–23 and 12b–32 under the Exchange Act (17 CFR 240.12b–23 and 240.12b–32) (additional rules on incorporation by reference for reports filed pursuant to Sections 13 and 15(d) of the Exchange Act); and Rules 0–4, 8b–23, and 8b–32 under the Act (17 CFR 270.0–4, 270.8b–23, and 270.8b–32) (additional rules on incorporation by reference for investment companies).

E. Definitions

Unless the context clearly indicates the contrary, terms used in this Form N–CSR have meanings as defined in the Act and the rules and regulations thereunder. Unless otherwise indicated, all references in the Form to statutory sections or to rules are sections of the Act and the rules and regulations thereunder.

F. Signature and Filing of Report

1. If the report is filed in paper pursuant to a hardship exemption from electronic filing (see Item 201 *et seq.* of Regulation S–T (17 CFR 232.201 *et seq.*)), eight complete copies of the report shall be filed with the Commission. At least one complete copy of the report shall be filed with each exchange on which any class of securities of the registrant is registered. At least one complete copy of the report filed with the Commission and one such copy filed with each exchange must be manually signed. Copies not manually signed must bear typed or printed signatures.

2. (a) The report must be signed by the registrant, and on behalf of the registrant by its principal executive officer or officers (who also must provide the certification required by Rule 30a–2 under the Act (17 CFR 270.30a–2) exactly as specified in this Form) and its principal financial officer or officers (who also must provide the certification required by Rule 30a–2 under the Act (17 CFR 270.30a–2) exactly as specified in this Form).

(b) The name of each person who signs the report shall be typed or printed beneath his or her signature. Any person who occupies more than one of the specified positions shall indicate each capacity in which he or she signs the report. Attention is directed to Rule 12b–11 under the Exchange Act (17 CFR 240.12b–11) and Rule 8b–11 under the Act (17 CFR 270.8b–11) concerning manual signatures and signatures pursuant to powers of attorney.

Item 1. Reports to Stockholders

Include a copy of the report transmitted to stockholders pursuant to Rule 30e–1 under the Act (17 CFR 270.30e–1).

Item 2. Code of Ethics

(a) Disclose whether, as of the end of the period covered by the report, the registrant has adopted a code of ethics that applies to the registrant's principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions, regardless of whether these individuals are employed by the registrant or a third party. If the registrant has not adopted such a code of ethics, explain why it has not done so.

Instruction to paragraph (a).

The information required by this Item is only required in an annual report on this Form N–CSR.

(b) For purposes of this Item, the term ''code of ethics'' means written standards that are reasonably designed to deter wrongdoing and to promote:

(1) Honest and ethical conduct, including the ethical handling of actual or apparent conflicts of interest between personal and professional relationships;

(2) Full, fair, accurate, timely, and understandable disclosure in reports and documents that a registrant files with, or submits to, the Commission and in other public communications made by the registrant;

(3) Compliance with applicable governmental laws, rules, and regulations;

(4) The prompt internal reporting of violations of the code to an appropriate person or persons identified in the code; and

(5) Accountability for adherence to the code.

(c) The registrant must briefly describe the nature of any amendment, during the period covered by the report, to a provision of its code of ethics that applies to the registrant's principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions, regardless of whether these individuals are employed by the registrant or a third party, and that relates to any element of the code of ethics definition enumerated in paragraph (b) of this Item. The registrant must file a copy of any such amendment as an exhibit pursuant to Item 10(a), unless the registrant has elected to satisfy paragraph (f) of this Item by posting its code of ethics on its website pursuant to paragraph (f)(2) of this Item, or by undertaking to provide its code of ethics to any person without charge, upon request, pursuant to paragraph (f)(3) of this Item.

(d) If the registrant has, during the period covered by the report, granted a waiver, including an implicit waiver,

from a provision of the code of ethics to the registrant's principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions, regardless of whether these individuals are employed by the registrant or a third party, that relates to one or more of the items set forth in paragraph (b) of this Item, the registrant must briefly describe the nature of the waiver, the name of the person to whom the waiver was granted, and the date of the waiver.

(e) If the registrant intends to satisfy the disclosure requirement under paragraph (c) or (d) of this Item regarding an amendment to, or a waiver from, a provision of its code of ethics that applies to the registrant's principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions and that relates to any element of the code of ethics definition enumerated in paragraph (b) of this Item by posting such information on its Internet website, disclose the registrant's Internet address and such intention.

(f) The registrant must:

(1) File with the Commission, pursuant to Item 10(a), a copy of its code of ethics that applies to the registrant's principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions, as an exhibit to its annual report on this Form N–CSR;

(2) Post the text of such code of ethics on its Internet website and disclose, in its most recent report on this Form N–CSR, its Internet address and the fact that it has posted such code of ethics on its Internet website; or

(3) Undertake in its most recent report on this Form N–CSR to provide to any person without charge, upon request, a copy of such code of ethics and explain the manner in which such request may be made.

Instructions to Item 2.

1. A registrant may have separate codes of ethics for different types of officers. Furthermore, a ''code of ethics'' within the meaning of paragraph (b) of this Item may be a portion of a broader document that addresses additional topics or that applies to more persons than those specified in paragraph (a). In satisfying the requirements of paragraph (f), a registrant need only file, post, or provide the portions of a broader document that constitutes a ''code of ethics'' as defined in paragraph (b) and that apply to the persons specified in paragraph (a).

2. If a registrant elects to satisfy paragraph (f) of this Item by posting its code of ethics on its website pursuant to paragraph (f)(2), the code of ethics must remain accessible on its website for as long as the registrant remains subject to the requirements of this Item and chooses to comply with this Item by posting its code on its website pursuant to paragraph (f)(2).

3. The registrant does not need to provide any information pursuant to paragraphs (c) and (d) of this Item if it discloses the required information on its Internet website within five business days following the date of the amendment or waiver and the registrant has disclosed in its most recently filed report on this Form N–CSR its Internet address and intention to provide disclosure in this manner. If the amendment or waiver occurs on a Saturday, Sunday, or holiday on which the Commission is not open for business, then the five business day period shall begin to run on and include the first business day thereafter. If the registrant elects to disclose this information through its website, such information must remain available on the website for at least a 12-month period. The registrant must retain the information for a period of not less than six years following the end of the fiscal year in which the amendment or waiver occurred. Upon request, the registrant must furnish to the Commission or its staff a copy of any or all information retained pursuant to this requirement.

4. The registrant does not need to disclose technical, administrative, or other non-substantive amendments to its code of ethics.

5. For purposes of this Item:

(a) The term ''waiver'' means the approval by the registrant of a material departure from a provision of the code of ethics; and

(b) The term ''implicit waiver'' means the registrant's failure to take action within a reasonable period of time regarding a material departure from a provision of the code of ethics that has been made known to an executive officer, as defined in Rule 3b–7 under the Exchange Act (17 CFR 240.3b–7), of the registrant.

Item 3. Audit Committee Financial Expert

(a)(1) Disclose that the registrant's board of directors has determined that the registrant either:

(i) Has at least one audit committee financial expert serving on its audit committee; or

(ii) Does not have an audit committee financial expert serving on its audit committee.

(2) If the registrant provides the disclosure required by paragraph (a)(1)(i) of this Item, it must disclose the name of the audit committee financial expert and whether that person is ''independent.'' In order to be considered ''independent'' for purposes of this Item, a member of an audit committee may not, other than in his or her capacity as a member of the audit committee, the board of directors, or any other board committee:

(i) Accept directly or indirectly any consulting, advisory, or other compensatory fee from the issuer; or

(ii) Be an ''interested person'' of the investment company as defined in Section 2(a)(19) of the Act (15 U.S.C. 80a–2(a)(19)).

(3) If the registrant provides the disclosure required by paragraph (a)(1)(ii) of this Item, it must explain why it does not have an audit committee financial expert.

Instructions to paragraph (a).

1. The information required by this Item is only required in an annual report on Form N–CSR.

2. If the registrant's board of directors has determined that the registrant has more than one audit committee financial expert serving on its audit committee, the registrant may, but is not required to, disclose the names of those additional persons. A registrant choosing to identify such persons must indicate whether they are independent pursuant to paragraph (a)(2) of this Item.

(b) For purposes of this Item, an ''audit committee financial expert'' means a person who has the following attributes:

(1) An understanding of generally accepted accounting principles and financial statements;

(2) The ability to assess the general application of such principles in connection with the accounting for estimates, accruals, and reserves;

(3) Experience preparing, auditing, analyzing, or evaluating financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of issues that can reasonably be expected to be raised by the registrant's financial statements, or experience actively supervising one or more persons engaged in such activities;

(4) An understanding of internal controls and procedures for financial reporting; and

(5) An understanding of audit committee functions.

(c) A person shall have acquired such attributes through:

(1) Education and experience as a principal financial officer, principal

accounting officer, controller, public accountant, or auditor or experience in one or more positions that involve the performance of similar functions;

(2) Experience actively supervising a principal financial officer, principal accounting officer, controller, public accountant, auditor, or person performing similar functions;

(3) Experience overseeing or assessing the performance of companies or public accountants with respect to the preparation, auditing, or evaluation of financial statements; or

(4) Other relevant experience.

(d)(1) A person who is determined to be an audit committee financial expert will not be deemed an ''expert'' for any purpose, including without limitation for purposes of Section 11 of the Securities Act of 1933 (15 U.S.C. 77k), as a result of being designated or identified as an audit committee financial expert pursuant to this Item.

(2) The designation or identification of a person as an audit committee financial expert pursuant to this Item does not impose on such person any duties, obligations, or liability that are greater than the duties, obligations, and liability imposed on such person as a member of the audit committee and board of directors in the absence of such designation or identification.

(3) The designation or identification of a person as an audit committee financial expert pursuant to this Item does not affect the duties, obligations, or liability of any other member of the audit committee or board of directors.

Instruction to Item 3.

If a person qualifies as an audit committee financial expert by means of having held a position described in paragraph (c)(4) of this Item, the registrant shall provide a brief listing of that person's relevant experience.

Items 4–8. [Reserved]

Item 9. Controls and Procedures

(a) Disclose the conclusions of the registrant's principal executive officer or officers and principal financial officer or officers, or persons performing similar functions, about the effectiveness of the registrant's disclosure controls and procedures (as defined in Rule 30a–2(c) under the Act (17 CFR 270.30a–2(c))) based on their evaluation of these controls and procedures as of a date within 90 days of the filing date of the report that includes the disclosure required by this paragraph.

(b) Disclose whether or not there were significant changes in the registrant's internal controls or in other factors that could significantly affect these controls subsequent to the date of their evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Item 10. Exhibits

File the exhibits listed below as part of this Form. Letter or number the exhibits in the sequence indicated.

(a) Any code of ethics, or amendment thereto, that is the subject of the disclosure required by Item 2, to the extent that the registrant intends to satisfy the Item 2 requirements through filing of an exhibit.

(b) A separate certification for each principal executive officer and principal financial officer of the registrant as required by Rule 30a–2 under the Act (17 CFR 270.30a–2) in the exact form set forth below:

Certifications

I, [identify the certifying individual], certify that:

1. I have reviewed this report on Form N–CSR of [identify registrant];

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations, changes in net assets, and cash flows (if the financial statements are required to include a statement of cash flows) of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Rule 30a–2(c) under the Investment Company Act of 1940) for the registrant and have:

(a) Designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this report (the ''Evaluation Date''); and

(c) presented in this report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize, and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

(b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: _____

_____

[Signature] [Title]

Signatures

[See General Instruction F]

Pursuant to the requirements of the Securities Exchange Act of 1934 and the Investment Company Act of 1940, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

(Registrant) _____

By (Signature and Title)* _____

Date _____

Pursuant to the requirements of the Securities Exchange Act of 1934 and the Investment Company Act of 1940, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

By (Signature and Title)* _____

Date _____

By (Signature and Title)* _____

_____

Date

* Print the name and title of each signing officer under his or her signature.

Dated: January 27, 2003.

By the Commission.

Margaret H. McFarland,

Deputy Secretary.

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