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17 CFR Parts 239, 249, 274, and 275
Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies and Investment Advisors; Proposed Rules

SECURITIES AND EXCHANGE COMMISSION

17 CFR Parts 239, 249, and 274

[Release Nos. 33–8131, 34–46518, IC–25739; File No. S7–36–02]

RIN 3235–AI64

Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rule.

SUMMARY: The Securities and Exchange Commission is proposing amendments to its forms under the Securities Act of 1933, the Securities Exchange Act of 1934, and the Investment Company Act of 1940 to require registered management investment companies to provide disclosure about how they vote proxies relating to portfolio securities they hold. Under the proposed amendments, registered management investment companies would be required to disclose the policies and procedures that they use to determine how to vote proxies relating to portfolio securities. The proposals also would require registered management investment companies to file with the Commission and to make available to their shareholders the specific proxy votes that they cast in shareholder meetings of issuers of portfolio securities.

DATES: Comments must be received on or before December 6, 2002.

ADDRESSES: To help us process and review your comments more efficiently, comments should be sent by one method only.

Comments should be submitted in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549–0609. Comments also may be submitted electronically at the following E-mail address: *rule-comments@sec.gov.* All comment letters should refer to File No. S7–36–02; this file number should be included in the subject line if electronic mail is used. Comment letters will be available for public inspection and copying in the Commission's Public Reference Room, 450 Fifth Street, NW., Washington, DC 20549. Electronically submitted comment letters also will be posted on the Commission's Internet Web site (*http://www.sec.gov*).[1]

FOR FURTHER INFORMATION CONTACT: Christian L. Broadbent, Attorney, Nicholas C. Milano, Jr., Senior Counsel, 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 proposing for comment amendments to Forms N–1A [17 CFR 239.15A; 274.11A], N–2 [17 CFR 239.14; 274.11a–1], and N–3 [17 CFR 239.17a; 17 CFR 274.11b], the registration forms used by management investment companies to register under the Investment Company Act of 1940 (''Investment Company Act'') and to offer their securities under the Securities Act of 1933 (''Securities Act''), and amendments to proposed Form N–CSR [17 CFR 249.331; 17 CFR 274.128], a form that we recently proposed under the Securities Exchange Act of 1934 (''Exchange Act'') and the Investment Company Act to be used by registered management investment companies to file certified shareholder reports with the Commission under the Sarbanes-Oxley Act of 2002.[2]

Executive Summary

We are proposing form amendments that would do the following:

- Require a management investment company registered under the Investment Company Act of 1940 (''fund'') to disclose in its registration statement (and, in the case of a closed-end fund, Form N–CSR) the policies and procedures that it uses to determine how to vote proxies relating to portfolio securities; and
- Require a fund to file with the Commission and make available to its shareholders, upon request and free of charge, the fund's proxy voting record. A fund would be required to disclose in its annual and semi-annual reports to shareholders and in its registration statement the methods by which shareholders may obtain information about proxy voting. A fund also would be required to disclose in its annual and semi-annual reports to shareholders information regarding any proxy votes that are inconsistent with its proxy voting policies and procedures.

In a companion release, we are also publishing proposed amendments that would require registered investment advisers to adopt and implement written policies and procedures reasonably designed to ensure that proxies are voted in the best interests of their clients, disclose to clients information about the advisers' proxy voting policies and procedures, disclose to clients how they may obtain information on how the adviser voted their proxies, and retain records relating to voting proxies on client securities.[3]

I. Introduction and Background

As of December 2001, mutual funds[4] held $3.4 trillion in U.S. corporate stock, representing approximately 19% of all publicly traded U.S. corporate equity.[5] This represents a dramatic increase from only 6.4% a decade earlier.[6] Millions of individual American investors, in turn, hold shares of equity mutual funds, relying on these funds —and the value of the corporate securities in which they invest—to fund their retirements, their childrens' educations, and their other basic financial needs.[7] Yet, despite the enormous influence of mutual funds in the capital markets and their huge impact on the financial fortunes of American investors, funds have been reluctant to disclose how they exercise their proxy voting power with respect to portfolio securities.[8] We believe that the

[1] We do not edit personal identifying information, such as names or electronic mail addresses, from electronic submissions. You should submit only information that you wish to make available publicly.

[2] *See* Investment Company Act Release No. 25723 (Aug. 30, 2002) [67 FR 57298 (Sept. 9, 2002)]; Sarbanes-Oxley Act of 2002, Pub. L. 107–204, 116 Stat. 745 (2002).

[3] *See* Investment Advisers Act Release No. 2059 (Sept. 20, 2002).

[4] For simplicity, this Section of the release focuses on mutual funds (*i.e.*, open-end management investment companies). An open-end management investment company is an investment company, other than a unit investment trust or face-amount certificate company, that offers for sale or has outstanding any redeemable security of which it is the issuer. *See* Sections 4 and 5(a)(1) of the Investment Company Act [15 U.S.C. 80a–4 and 80a–5(a)(1)]. Our proposed amendments, however, would apply to all registered management investment companies, except where noted. This includes both closed-end management investment companies and insurance company separate accounts organized as management investment companies that offer variable annuity contracts.

[5] Investment Company Institute, Mutual Fund Fact Book 62 (42nd ed. 2002); Securities Industry Association, Securities Industry Fact Book 71 (2002).

[6] Securities Industry Fact Book, *supra* note , at 71.

[7] Mutual Fund Fact Book, *supra* note , at 37. Approximately 93 million individual investors hold shares of mutual funds. *Id.* Shares of equity mutual funds are held through 164.8 million shareholder accounts. *Id.* at 63. A single individual may hold mutual fund shares through multiple accounts.

[8] *See* John Wasik, *Speak Loudly—Or Lose Your Big Stick,* The Financial Times, July 24, 2002, at 26 (only eight retail mutual fund groups that openly disclose how they vote on proxies). We have previously prepared reports commenting on the role of institutional investors in the corporate accountability process and their impact on portfolio companies. See Division of Corporation Finance, SEC, Staff Report on Corporate Accountability (Sept. 4, 1980) (printed for the use of Senate Comm. on Banking, Housing and Urban Affairs, 96th Cong., 2d Sess.) (hereinafter SEC, Staff Report on

time has come to consider increasing transparency of proxy voting by mutual funds. This increased transparency would enable fund shareholders to monitor their funds' involvement in the governance activities of portfolio companies, which could have a dramatic impact on shareholder value.[9]

Mutual funds are formed as corporations or business trusts under state law and, as in the case of other corporations and trusts, must be operated for the benefit of their shareholders.[10] Because a mutual fund is the beneficial owner of its portfolio securities, the fund's board of directors, acting on the fund's behalf, has the right and the obligation to vote proxies relating to the fund's portfolio securities. As a practical matter, however, the board generally delegates this function to the fund's investment adviser as part of the adviser's general management of fund assets, subject to the board's continuing oversight. The investment adviser to a mutual fund is a fiduciary that owes the fund a duty of ''utmost good faith, and full and fair disclosure.'' [11] This fiduciary duty extends to all functions undertaken on the fund's behalf, including the voting of proxies relating to the fund's portfolio securities. An investment adviser voting proxies on behalf of a fund, therefore, must do so in a manner consistent with the best interests of the fund and its shareholders.[12]

Traditionally, mutual funds have been viewed as largely passive investors, reluctant to challenge corporate management on issues such as corporate governance.[13] Funds have often followed the so-called ''Wall Street rule,'' according to which an investor should either vote as management recommends or, if dissatisfied with management, sell the stock.[14] In recent years, however, some funds, along with other institutional investors, have become more assertive in exercising their proxy voting responsibilities.[15] The increased assertiveness by mutual funds in the voting of proxies may have a number of causes. In some instances, funds have come to hold such large positions in a particular portfolio company that they cannot easily sell the company's stock if the company's management is performing poorly.[16] The investment policies of index funds generally do not permit them to sell poorly performing investments, and thus these funds may become active in corporate governance in order to maximize value for their shareholders.[17]

Recent corporate scandals have created renewed investor interest in issues of corporate governance and have underscored the need for mutual funds and other institutional investors to play a more active role in corporate governance.[18] The increased equity holdings and accompanying voting power of mutual funds place them in a position to have enormous influence on corporate accountability. As major shareholders, mutual funds may play a vital role in monitoring the stewardship of the companies in which they invest.

Moreover, in some situations the interests of a mutual fund's shareholders may conflict with those of its investment adviser with respect to proxy voting.[19] This may occur, for example, when a fund's adviser also manages or seeks to manage the retirement plan assets of a company whose securities are held by the fund.[20] In these situations, a fund's adviser may have an incentive to support management recommendations to further its business interests.

Yet, in spite of the substantial institutional voting power held by mutual funds, the increasing importance of the exercise of that power to fund shareholders, and the potential for conflicts of interest with respect to the exercise of fund proxy voting power, limited information is available regarding how funds vote their proxies. At present, the Commission's rules do not require mutual funds to disclose either their proxy voting policies and procedures or their proxy voting records.[21] Several mutual fund complexes voluntarily provide information to investors, often on their websites, about the policies and procedures that they use to determine

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Corporate Accountability); SEC, Institutional Investor Study Report (Mar. 10, 1971) (printed for the use of House Comm. on Interstate and Foreign Commerce, 92nd Cong., 1st Sess.) (hereinafter SEC, Institutional Investor Study Report).

[9] We have received three rulemaking petitions urging that we adopt rules requiring funds to disclose both the policies and guidelines followed by the funds in determining how to vote on proxy proposals, and the record of actual proxy votes cast. *See* Rulemaking Petition by Domini Social Investments, LLC (Nov. 27, 2001); Rulemaking Petition by the International Brotherhood of Teamsters (Jan. 18, 2001); Rulemaking Petition by the American Federation of Labor and Congress of Industrial Organizations (July 30, 2002 and Dec. 20, 2000). The rulemaking petitions are available for inspection and copying in File No. 4–439 in the Commission's Public Reference Room.

[10] *See generally* James M. Storey & Thomas M. Clyde, Mutual Fund Law Handbook § 7.2 (1998); Allan S. Mostoff & Olivia P. Adler, *Organizing an Investment Company—Structural Considerations* § 2.4 *in* The Investment Company Regulation Deskbook (Amy L. Goodman ed., 1997).

[11] *SEC* v. *Capital Gains Research Bureau, Inc.,* 375 U.S. 180, 194 (1963) (interpreting Section 206 of the Investment Advisers Act of 1940). *Cf.* Section 36(b) of the Investment Company Act [15 U.S.C. 80a–35] (investment adviser of a fund has a fiduciary duty with respect to the receipt of compensation paid by the fund).

[12] *See* Investment Advisers Act Release No. 2059, *supra* note . *See also* SEC, Staff Report on Corporate Accountability, *supra* note , at 391 (fiduciary principle applies to all aspects of investment management, including voting). *Cf.* Dep't of Labor, Interpretive Bulletins Relating to the Employee Retirement Income Security Act of 1974, 29 CFR 2509.94–2 (2002) (fiduciary act of managing employee benefit plan assets consisting of equity securities includes voting of proxies appurtenant to those securities).

[13] *See, e.g.*, SEC, Staff Report on Corporate Accountability, *supra* note 8, at 404 (investment managers have routinely supported management slates of director nominees); Alan R. Palmiter, *Mutual Fund Voting of Portfolio Shares: Why Not Disclose?*, 23 Cardozo L. Rev. 1419, 1430–31 (2002) (discussing mutual fund passivity in corporate governance). *See generally* John C. Coffee, Jr., *The SEC and The Institutional Investor: A Half-Time Report,* 15 Cardozo L. Rev. 837 (1994) (institutional investors have historically been passive investors); Bernard S. Black, *Shareholder Passivity Reexamined,* 89 Mich. L. Rev. 520 (1990) (shareholder voting has historically been passive).

[14] *See* SEC, Staff Report on Corporate Accountability, *supra* note 8, at 392 (describing ''Wall Street Rule'').

[15] *See, e.g.*, Aaron Lucchetti, *A Mutual-Fund Giant Is Stalking Excessive Pay,* Wall Street Journal, June 12, 2002, at C1 (Fidelity has voted against management recommendations involving stock-option plans); Kathleen Day, *Prodding For Disclosure of Funds' Proxy Votes,* Washington Post, Apr. 8, 2001, at H1 (Domini Social Equity Fund voted against management proposal to issue additional stock options for directors).

[16] *See* Palmiter, *supra* note 13, at 1435–1436 (as holdings have increased, mutual funds have realized that they cannot easily sell blocks of poorly performing stock).

[17] *See* Kathleen Pender, *The Influence of Indexing on the Markets,* San Francisco Chronicle, June 23, 2002, at G1 (some index funds are more likely to vote proxies because they generally cannot sell portfolio securities consistent with their investment policies).

[18] *See, e.g.*, Josh Friedman, *Vanguard to Turn More Activist in Proxy Voting,* Los Angeles Times, Aug. 22, 2002, at B3 (Vanguard imposing stricter corporate governance guidelines in light of recent events); Tom Hamburger, *Union Targets Corporate Change,* Wall Street Journal, July 30, 2002, at A2 (workers should use pension funds and votes to compel changes in corporate behavior); Beth Healy, *Big Investors Assuming a More Activist Stance,* Boston Globe, July 11, 2002, at C1 (big investors say they are taking a more activist stance after financial scandals at Enron, Global Crossing, and WorldCom); Russ Wiles, *Funds May Have More to Say on Governance,* Chicago Sun-Times, June 3, 2002, at F53 (investors taking a closer look at corporate governance issues as a result of Enron).

[19] *See, e.g.*, Aaron Bernstein & Geoffrey Smith, *Can You Trust Your Fund Company?,* BusinessWeek Online, Aug. 8, 2002 (AFL–CIO argues that conflicts of interest lead mutual funds to vote with management).

[20] For additional examples of potential conflicts of interest involving investment advisers, see Investment Advisers Act Release No. 2059, *supra* note 3, at Section I., ''Background.''

[21] In general, investment companies are organized either as business trusts in Delaware or Massachusetts, or as corporations in Maryland. The applicable state statutes do not specifically permit shareholders to inspect books and records relating to proxy voting by funds with respect to portfolio securities. *See* Del. Code Ann. tit. 12, § 3801–3824 (2001); Mass. Gen. Laws. Ann. ch. 182, § 1–14 (2002); Md. Code Ann., Corporations § 2–512 (2001).

how to vote proxies and, in some cases, their actual proxy voting decisions.[22] The Internet provides a medium for these funds to make information about their proxy voting available to shareholders quickly and in a cost-effective manner. We applaud these voluntary efforts of mutual funds to disclose proxy voting information to shareholders, and we encourage all funds to provide similar information without delay.

We believe, however, that the time has now arrived for the Commission to consider requiring mutual funds to disclose their proxy voting policies and procedures, and their actual voting records.[23] Proxy voting decisions by funds may play an important role in maximizing the value of the funds' investments, having an enormous impact on the financial livelihood of millions of Americans. Further, requiring greater transparency of proxy voting by funds may encourage funds to become more engaged in corporate governance of issuers held in their portfolios, which may benefit all investors and not just fund shareholders. Finally, shedding light on mutual fund proxy voting could illuminate potential conflicts of interest and discourage voting that is inconsistent with fund shareholders' best interests. Advances in technology over the last 30 years, specifically the Internet, allow this disclosure of proxy voting records to be readily accessible at low cost.

II. Discussion

We are proposing to amend the registration forms for funds, and recently proposed Form N–CSR, to require the disclosure of fund proxy voting policies and procedures as well as actual proxy votes cast.[24]

A. Disclosure of Policies and Procedures With Respect To Voting Proxies Relating to Portfolio Securities

We are proposing to require funds that invest in voting securities to disclose in their statements of additional information (''SAIs'') the policies and procedures that they use to determine how to vote proxies relating to securities held in their portfolios.[25] This would include the procedures that a fund uses when a vote presents a conflict between the interests of fund shareholders, on the one hand, and those of the fund's investment adviser, principal underwriter, or any affiliated person of the fund, its investment adviser, or principal underwriter, on the other. It also would include any policies and procedures of a fund's investment adviser, or any other third party, that the fund uses, or that are used on the fund's behalf, to determine how to vote proxies relating to portfolio securities.[26] For example, if a fund delegates proxy voting decisions to its investment adviser and the adviser uses its own policies and procedures to vote the fund's proxies, disclosure of the adviser's policies and procedures would be required.

For open-end management investment companies that continuously offer their shares and maintain an updated registration statement, the required SAI disclosure will result in continuous investor access, upon request, to current proxy voting policies and procedures. Because closed-end funds do not offer their shares continuously, and are therefore generally not required to maintain an updated SAI to meet their obligations under the Securities Act of 1933,[27] we are also proposing to require closed-end funds to disclose their proxy voting policies and procedures annually on Form N–CSR.[28]

We would expect that funds' disclosure of their policies and procedures would include general policies and procedures, as well as policies with respect to voting on specific types of issues. The following are examples of general policies and procedures that some funds include in their proxy voting policies and procedures and with respect to which disclosure would be appropriate:

- The extent to which the fund delegates its proxy voting decisions to its investment adviser or another third party, or relies on the recommendations of a third party;
- Policies and procedures relating to matters that may affect substantially the rights or privileges of the holders of securities to be voted; and
- Policies regarding the extent to which the fund will support or give weight to the views of management of the company.

The following are examples of specific types of issues that are covered by some funds' proxy voting policies and procedures and with respect to which disclosure would be appropriate:

- Corporate governance matters, including changes in the state of incorporation, mergers and other

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[22] *See* Calvert Group, Ltd. <*www.calvertgroup.com*> (visited July 25, 2002) (proxy voting policies and votes cast); Domini Social Investments LLC <*www.domini.com*> (visited July 25, 2002) (proxy voting policies and votes cast); Fidelity Management & Research Company <*www.fidelity.com* > (visited Sept. 4, 2002) (proxy voting policies); PAX World Management Corporation <*www.paxfund.com*> (visited July 25, 2002) (proxy voting policies and votes cast); Teachers Insurance and Annuity Association of America-College Retirement and Equities Fund <*www.tiaa-cref.org*> (visited Sept. 8, 2002) (proxy voting policies); The Vanguard Group <*www.vanguard.com*> (visited Sept. 5, 2002) (proxy voting policies).

[23] Twice in the past we have considered requiring funds to provide information about proxy voting with respect to portfolio securities. *See* Notice of Proposal to Amend Forms N–8B–1, N–8B–3, N–8B–4, N–5, and N–1Q To Require Registered Investment Companies To Disclose with Greater Specificity Their Policies on Involvement In the Affairs of Their Portfolio Companies, Investment Company Act Release No. 6853 (Dec. 1, 1971) [36 FR 25434 (Dec. 31, 1971)] (proposed amendments would have required registered investment companies to disclose their policies and procedures for considering proxy materials of portfolio companies); Notice of Withdrawal of Proposal to Amend Forms N–8B–1, N–8B–3, N–8B–4, N–5, and N–1Q To Require Registered Investment Companies To Disclose with Greater Specificity Their Policies on Involvement In the Affairs of Their Portfolio Companies, Investment Company Act Release No. 9295 (May 20, 1976) [41 FR 21796 (May 28, 1976)]; Proposed Rules Relating to Shareholder Communications, Shareholder Participation in the Corporate Electoral Process and Corporate Governance Generally, Securities Exchange Act Release No. 14970 (July 18, 1978) [43 FR 31945 (July 24, 1978)] (proposed rules would have required registered investment companies and other institutional investors to disclose their proxy voting policies and procedures for equity securities held for their own account or the account of others, and the number of times they voted for or against management or abstained from voting on any contested matter); Proposed Rules Relating to Shareholder Communications, Shareholder Participation in the Corporate Electoral Process and Corporate Governance Generally, Withdrawal of Proposed Rule and Amendments, Securities Exchange Act Release No. 15385 (Dec. 6, 1978) [43 FR 58533 (Dec. 14, 1978)]. In 2000, we proposed amendments to Form ADV, the registration form for investment advisers, that would require registered investment advisers to disclose their proxy voting practices. *See* Electronic Filing by Investment Advisers; Proposed Amendments to Form ADV, Investment Advisers Act Release No. 1862 (Apr. 5, 2000) [65 FR 20524 (Apr. 17, 2000)]. These amendments remain pending.

[24] Form N–1A [17 CFR 239.15A; 17 CFR 274.11A] is the registration form for open-end management investment companies. Form N–2 [17 CFR 239.14; 17 CFR 11a–1] is the registration form for closed-end management investment companies. Form N–3 [17 CFR 239.17a; 17 CFR 274.11b] is the registration form for separate accounts organized as management investment companies that offer variable annuity contracts.

[25] The SAI is part of a fund's registration statement and contains information about a fund in addition to that contained in the prospectus. The SAI is required to be delivered to investors upon request and is available on the Commission's Electronic Data Gathering, Analysis, and Retrieval System (''EDGAR'').

[26] Proposed Item 13(f) of Form N–1A; Proposed Item 18.16 of Form N–2; Proposed Item 20(o) of Form N–3. *See* Section 2(a)(3) of the Investment Company Act [15 U.S.C. 80a–2(a)(3)] (defining affiliated person).

[27] Pursuant to rule 8b–16(b) under the Investment Company Act [17 CFR 270.8b–16(b)], closed-end funds are not required to file amendments to their registration statements (including their SAIs) in order to comply with their Investment Company Act registration obligations, provided that they include specified information in their annual reports to shareholders.

[28] Item 3 of proposed Form N–CSR.

corporate restructurings, and anti-takeover provisions such as staggered boards, poison pills, and supermajority provisions;

- Changes to capital structure, including increases and decreases of capital and preferred stock issuance;
- Stock option plans and other management compensation issues; and
- Social and corporate responsibility issues.

We also are proposing to require that a fund disclose in its shareholder reports that a description of the fund's proxy voting policies and procedures is available (i) without charge, upon request, by calling a specified toll-free (or collect) telephone number; (ii) on the fund's website, if applicable; and (iii) on the Commission's Web site at *http://www.sec.gov*.[29] The proposals also would require a fund to send this description of the fund's proxy voting policies and procedures within three business days of receipt of the request, by first-class mail or other means designed to ensure equally prompt delivery.[30]

We request comment generally on the disclosure of policies and procedures that funds use to determine how to vote proxies relating to securities held in their portfolios and specifically on the following issues.

- Should we require funds to disclose their policies and procedures with respect to voting proxies of portfolio securities?
- Should we provide greater specificity with regard to the disclosure that funds are required to make? For example, should our forms expressly require disclosure of any or all of the specific matters enumerated above or of any other specific matters?
- Is the SAI (and, for closed-end funds, Form N–CSR) the appropriate location for funds to disclose their policies and procedures with respect to voting proxies relating to portfolio securities? Will our proposals provide adequate access to fund proxy voting policies and procedures by fund shareholders and prospective investors? Should the disclosure be included in a document that is delivered to every shareholder?

B. Disclosure of Proxy Voting Record

We also are proposing to require each fund to file with the Commission its proxy voting record and make this record available to its shareholders. In addition, a fund would be required to disclose in its annual and semi-annual reports to shareholders information regarding any proxy votes that are inconsistent with its proxy voting policies and procedures.

Disclosure of Complete Proxy Voting Record

The Commission is proposing to require a fund to file its complete proxy voting record as part of its report on proposed Form N–CSR. Today's proposals would add a new item to proposed Form N–CSR, which would require a fund to disclose the following information for each matter relating to a portfolio security considered at any shareholder meeting held during the period covered by the report and with respect to which the fund was entitled to vote:

- The name of the issuer of the portfolio security;
- The exchange ticker symbol of the portfolio security;
- The Council on Uniform Securities Identification Procedures (''CUSIP'') number for the portfolio security;
- The shareholder meeting date;
- A brief identification of the matter voted on;
- Whether the matter was proposed by the issuer or by a security holder;
- Whether the fund cast its vote on the matter;
- How the fund cast its vote (*e.g.*, for or against proposal, or abstain; for or withhold regarding election of directors); and
- Whether the fund cast its vote for or against management.[31]

A fund also would be required to make its proxy voting record available to its shareholders. Specifically, the proposals would require a fund to disclose in its SAI, as well as annual and semi-annual reports to shareholders, that the fund's proxy voting record is available (i) without charge, upon request, by calling a specified toll-free (or collect) telephone number, (ii) on the fund's Web site, if applicable, and (iii) on the Commission's Web site.[32] The proposals also would require a fund, upon receipt of a request for its proxy voting record, to send the information disclosed in response to Item 2 of the Fund's most recently filed Form N–CSR.[33] Funds would be required to send this information within three business days of receipt of the request, by first-class mail or other means designed to ensure equally prompt delivery.[34]

Our proposals would require that a fund's proxy voting policies and procedures and proxy voting record be publicly available through filings with us. They also would require that this information be readily available to fund shareholders, without charge, and that shareholders be apprised of how this information may be obtained. We believe that these proposals strike an appropriate balance—ensuring that a description of a fund's proxy voting policies and procedures, as well as its proxy voting record, are readily available to interested fund shareholders without imposing on funds, and their shareholders, unnecessary costs that would be associated with the distribution of this information to every shareholder of a fund.[35]

We considered whether to provide funds greater flexibility in determining the medium through which to make their proxy voting information available to their shareholders, so that a fund could, for example, meet this obligation exclusively through website access. We concluded that, at this time, requiring funds to make the information available to investors who call a toll-free (or collect) telephone number would ensure the most widespread access to this information by all investors. While the percentage of households with Internet access has increased considerably in recent years, it remains substantially lower than the percentage with access to telephones.[36]

We note, however, that we have taken steps to encourage issuers and market intermediaries to communicate with and deliver information to investors

[29] *See* Proposed Item 22(b)(7) and 22(c)(5) of Form N–1A; Proposed Instructions 4.g. & 5.e. to Item 23 of Form N–2; Proposed Instructions 4(vii) & 5(v) to Item 27(a) of Form N–3.

[30] Proposed Instructions to Items 22(b)(7) and 22(c)(5) of Form N–1A; Proposed Instruction 6 to Item 23 of Form N–2; Proposed Instruction 6 to Item 27(a) of Form N–3.

[31] Item 2 of proposed Form N–CSR.

[32] *See* Proposed Items 13(f) and 22(b)(7) & (c)(5) of Form N–1A; Proposed Item 18.16 and Proposed Instructions 4.g. and 5.e. to Item 23 of Form N–2; Proposed Item 20(o) and Proposed Instructions 4(vii) and 5(v) to Item 27(a) of Form N–3.

[33] Proposed Instructions to Items 13(f), 22(b)(7), and 22(c)(5) of Form N–1A; Proposed Instruction to Item 18.16 and proposed Instruction 6 to Item 23 of Form N–2; Proposed Instruction to Item 20(o) and proposed Instruction 6 to Item 27(a) of Form N–3.

[34] Id.

[35] *Cf.* Rulemaking Petition by Domini Social Investments, LLC (Nov. 27, 2001); Rulemaking Petition by the International Brotherhood of Teamsters (Jan. 18, 2001); Rulemaking Petition by the American Federation of Labor and Congress of Industrial Organizations (July 30, 2002, and Dec. 20, 2000) (requesting that the Commission require funds to provide their proxy voting information on the Internet and make paper copies available upon request).

[36] *See* Economics and Statistics Administration & National Telecommunications and Information Administration, A Nation Online: How Americans Are Expanding Their Use of the Internet, at 3 (Feb. 2002) (50.5% of households had Internet access as of Sept. 2001); Federal Communications Commission, Telephone Subscribership In the United States, at 1 (Feb. 2002) (95.1% of households had telephone service as of July 2001).

through the Internet.[37] The increased availability of information through the Internet has helped to promote transparency, liquidity, and efficiency by making information available to investors quickly and in a cost-effective manner. We encourage each fund to make its proxy voting information available to its shareholders on its website, if it has one.

We request comment generally on the proposed disclosure of a fund's proxy voting record and specifically on the following issues.

- What would be the costs of requiring funds to file with the Commission their proxy voting records on Form N–CSR, and to make these records available to their shareholders? Are there less costly alternative means of requiring funds to disclose their proxy voting records?
- What would be the benefits to fund shareholders and others of having funds' proxy voting records disclosed?
- Is Form N–CSR the appropriate location for the disclosure of a fund's proxy voting record? We have proposed, but not yet adopted, Form N–CSR. If we ultimately do not adopt Form N–CSR to implement the certification requirement of Section 302 of the Sarbanes-Oxley Act of 2002, should we nevertheless adopt Form N–CSR as a medium for a fund to disclose its proxy voting record? If not, how should a fund file its proxy voting record with the Commission? Should the information simply be filed together with the reports to shareholders currently required to be filed with the Commission pursuant to rule 30b2–1 under the Investment Company Act?[38]
- Is it sufficient to require that a fund's proxy voting record be made available to investors or should we require a fund to deliver its proxy voting record to each investor? For example, should a fund's complete proxy voting record be included in its reports to shareholders?
- Should a fund be permitted to meet its obligation to disclose its proxy voting record exclusively through posting the required information on its website?
- The proposal would require funds to disclose their proxy voting records semi-annually. Will this provide sufficiently frequent disclosure to investors? Should we require funds to disclose their proxy voting records more frequently? If so, through what means? Would less frequent disclosure, *e.g.*, annually, be sufficient?
- Are we proposing to require too much or too little information to be disclosed in proposed Form N–CSR? For example, should we limit the disclosure to contested matters, not require disclosure with respect to any categories of ''routine'' matters, or otherwise limit the types of matters with respect to which disclosure is required? Could funds generically disclose their votes on any categories of matters, *e.g.*, votes with management (or votes as recommended by an independent third-party proxy voting service) on certain categories of issues? Would this type of summary disclosure provide investors with adequate information? Should we require additional information, *e.g.*, information about how other funds in the fund complex have voted?
- Our proposed requirements to disclose proxy voting policies and procedures and proxy voting records would only apply to registered management investment companies. Should the proposed disclosure requirements also extend to unit investment trusts (''UITs'')?[39] If so, how should they apply? UITs do not include SAIs in their registration statements.[40] In addition, UITs do not transmit reports to shareholders.[41] Likewise, we have not proposed that UITs file proposed Form N–CSR. If the proxy voting disclosure requirements were to extend to UITs, where, and how frequently, should they make the required disclosure of their proxy voting policies and procedures and proxy voting records (*e.g.*, prospectus, annual report on Form N–SAR, a newly created form, sponsor's website)? How would UITs alert investors to the availability of the information since they do not file SAIs, or transmit reports to shareholders? Should UITs only be required to disclose proxy voting information annually because, unlike management investment companies, they are not currently subject to semi-annual reporting requirements? Are there any other modifications to the proposed disclosure requirements that would be appropriate in the case of UITs? If we extend the proposed proxy voting requirements to UITs, should we exempt UITs that invest exclusively in mutual funds, such as UITs that offer variable annuities and variable life insurance, since the underlying mutual funds would be covered?

Disclosure of Proxy Votes That Are Inconsistent With Fund's Policies and Procedures

We also are proposing to require a fund to disclose in its annual and semi-annual reports to shareholders proxy votes (or failures to vote) that are inconsistent with the fund's proxy voting policies and procedures.[42] The information that would be required would include the same information required by proposed Form N–CSR with respect to disclosure of the fund's complete proxy voting record.[43] In addition, the fund would be required to disclose the reasons why the fund voted, or failed to vote, in a manner inconsistent with its proxy voting policies and procedures.[44]

We believe that when a fund votes the proxies of its portfolio securities in a manner inconsistent with the fund's stated policies and procedures, a heightened risk exists that a conflict of interest may be present. Therefore, in these instances, it is appropriate that funds include information about the vote in reports that are delivered to all shareholders. We believe that this will provide shareholders with the best opportunity to evaluate the propriety of the proxy voting decision and will serve as a strong deterrent to voting decisions that are not in the best interests of shareholders.

We request comment generally on the disclosure of proxy votes that are inconsistent with a fund's policies and procedures and specifically on the following issues.

- Should we require disclosure in reports to shareholders of proxy votes

[37] *See, e.g.*, Acceleration of Periodic Report Filing Dates and Disclosure Concerning Website Access to Reports, Securities Act Release No. 8128 (Sept. 5, 2002) [67 FR 58479 (Sept. 16, 2002)] (requiring companies to include disclosure in their annual reports on Form 10–K about availability on company websites of reports on Forms 10–K, 10–Q, and 8–K).

[38] 17 CFR 270.30b2–1.

[39] A unit investment trust is ''an investment company which (A) is organized under a trust indenture, contract of custodianship or agency, or similar instrument, (B) does not have a board of directors, and (C) issues only redeemable securities, each of which represents an undivided interest in a unit of specified securities; but does not include a voting trust.'' Section 4(2) of the Investment Company Act [15 U.S.C. 80a–4(2)].

[40] Currently, UITs register under the Investment Company Act on Form N–8B–2 [17 CFR 274.12] and register their securities under the Securities Act of 1933 on Form S–6 [17 CFR 239.16].

[41] *Cf.* Rule 30e–2 under the Investment Company Act [17 CFR 270.30e–2] (requiring registered unit investment trusts substantially all of the assets of which consist of securities issued by a management investment company to transmit to their shareholders semi-annually a report containing all of the applicable information and financial statements or their equivalent required to be included in reports of the management investment company for the same fiscal period).

[42] *See* Proposed Items 22(b)(8) & (c)(6) of Form N–1A; Proposed Instructions 4.h. & 5.f. to Item 23 of Form N–2; Proposed Instructions 4(viii) & 5(vi) to Item 27(a) of Form N–3.

[43] *See* Item 2 of proposed Form N–CSR. *See also* discussion supra Section II.B., ''Disclosure of Complete Proxy Voting Record.''

[44] *See* Proposed Items 22(b)(8)(x) & (c)(6)(x) of Form N–1A; Proposed Instructions 4.h.(10) & 5.f.(10) to Item 23 of Form N–2; Proposed Instructions 4(viii)(J) & 5(vi)(J) to Item 27(a) of Form N–3.

that are inconsistent with a fund's proxy voting policies and procedures? Is it necessary or appropriate to require delivery (as opposed to availability) of this information to all shareholders?

• Should information about any other aspects of a fund's actual proxy voting record be required to be included in reports to shareholders? For example, should a fund be required to include in its reports to shareholders its votes on contested matters, management compensation issues, director elections, or any other matters?

III. General Request for Comments

The Commission requests comment on the amendments proposed in this release, whether any further changes to our rules or forms are necessary or appropriate to implement the objectives of our proposed amendments, and on other matters that might have an effect on the proposals contained in this release.

IV. Paperwork Reduction Act

Certain provisions of the proposed amendments contain ''collection of information'' requirements within the meaning of the Paperwork Reduction Act of 1995 [44 U.S.C. 3501, *et seq.*], and the Commission is submitting the proposed collections of information to the Office of Management and Budget (''OMB'') for review in accordance with 44 U.S.C. 3507(d) and 5 CFR 1320.11. The titles for the collections of information are: (1) ''Form N–1A under the Investment Company Act of 1940 and Securities Act of 1933, Registration Statement of Open-End Management Investment Companies'; (2) ''Form N–2—Registration Statement of Closed-End Management Investment Companies''; (3) ''Form N–3—Registration Statement of Separate Accounts Organized as Management Investment Companies''; and (4) ''Form N–CSR—Certified Shareholder Report of Registered Management Investment Companies.'' An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid OMB control number.

Form N–1A (OMB Control No. 3235–0307), Form N–2 (OMB Control No. 3235–0026), and Form N–3 (OMB Control No. 3235–0316) were adopted pursuant to Section 8(a) of the Investment Company Act [15 U.S.C. 80a–8] and Section 5 of the Securities Act [15 U.S.C. 77e]. We issued a release proposing Form N–CSR on August 30, 2002, pursuant to Section 8(a) of the Investment Company Act [15 U.S.C. 80a–8] and Section 13 of the Securities Exchange Act [15 U.S.C. 78m].

We are proposing amendments to require funds holding equity securities to disclose the policies and procedures that they use to determine how to vote the proxies of their portfolio securities. We are also proposing to require disclosure of the actual voting record with respect to such proxies. We believe that the changes we propose today will enhance the transparency of fund proxy voting and will allow shareholders to monitor whether funds are voting portfolio securities in the best interests of shareholders.

Form N–1A

Form N–1A, including the proposed amendments, contains collection of information requirements. The likely respondents to this information collection are open-end funds registering with the Commission on Form N–1A. Compliance with the disclosure requirements of Form N–1A is mandatory. Responses to the disclosure requirements are not confidential.

The current hour burden for preparing an initial Form N–1A filing is 801 hours per portfolio. The current annual hour burden for preparing post-effective amendments of Form N–1A is 99 hours per portfolio. The Commission estimates that, on an annual basis, 193 portfolios file initial registration statements on Form N–1A and 7,525 file post-effective amendments on Form N–1A. Thus, the current total annual hour burden for the preparation and filing of Form N–1A is 899,568 hours.

We estimate that the proposed amendments would increase the hour burden per portfolio per filing of an initial registration statement by 8 hours and would increase the hour burden per portfolio per filing of a post-effective amendment to a registration statement by 2 hours. Thus, if the proposed amendments to Form N–1A are adopted, the total annual hour burden for all funds for preparation and filing of initial registration statements and post-effective amendments to Form N–1A would be 916,162 hours.

Form N–2

Form N–2, including the proposed amendments, contains collection of information requirements. The likely respondents to this information collection are closed-end funds registering with the Commission on Form N–2. Compliance with the disclosure requirements of Form N–2 is mandatory. Responses to the disclosure requirements are not confidential.

The current hour burden for preparing an initial Form N–2 filing is 536.7 burden hours per filing, and the current annual hour burden for preparing post-effective amendments of Form N–2 is 101.7 hours per filing. The Commission currently estimates that, on an annual basis, 140 respondents file an initial registration statement on Form N–2 and 38 file post-effective amendments on Form N–2. Thus, the current total annual hour burden for the preparation and filing of Form N–2 is 79,003 hours.

We estimate that the proposed amendments would increase the hour burden per filing of an initial registration statement by 8 hours and would increase the hour burden per filing of a post-effective amendment to a registration statement by 2 hours. Thus, if the proposed amendments to Form N–2 are adopted, the total annual hour burden for all funds for preparation and filing of initial registration statements and post-effective amendments on Form N–2 would be 80,198.6 hours.

Form N–3

Form N–3, including the proposed amendments, contains collection of information requirements. The likely respondents to this information collection are separate accounts, organized as management investment companies and offering variable annuities, registering with the Commission on Form N–3. Compliance with the disclosure requirements of Form N–3 is mandatory. Responses to the disclosure requirements are not confidential.

The current annual hour burden for preparing an initial registration statement on a Form N–3 is 907.2 hours per portfolio. The current annual hour burden for preparing post-effective amendments of Form N–3 is 148.4 hours per portfolio. The Commission estimates that, on an annual basis, no initial registration statements will be filed on Form N–3 and 60 post-effective amendments will be filed on Form N–3. The estimated average number of portfolios per filing is 4, bringing the estimated total number of portfolios in post-effective amendments to Form N–3 filings annually to 240. Thus, the current total burden hours for the preparation and filing of Form N–3 is 35,616 hours.

We estimate that the proposed amendments would increase the hour burden per portfolio of an initial registration statement by 8 hours and would increase the hour burden per portfolio of a post-effective amendment to a registration statement by 2 hours. Thus, if the proposed amendments to Form N–3 are adopted, the total annual hour burden for all funds for preparation and filing of initial

registration statements and post-effective amendments on Form N–3 would be 36,096 hours.

Form N–CSR

Proposed Form N–CSR, including the proposed amendments, contains collection of information requirements. The respondents to this information collection would be management investment companies subject to rule 30e–1 under the Investment Company Act of 1940 registering with the Commission on Forms N–1A, N–2, or N–3. Compliance with the disclosure requirements of Form N–CSR is proposed to be mandatory. Responses to the disclosure requirements are not confidential.

We previously estimated that the hour burden for preparing a proposed Form N—CSR would be 5 hours per filing. We also estimated that 3,700 registered investment companies would file Form N–CSR on a semi-annual basis for a total of 7,400 filings. Thus, we estimated that the total annual hour burden for the preparation and filing of Form N–CSR would be 37,000 hours.[45]

We estimate that the proposed amendments would increase the hour burden per filing of a Form N–CSR by 10 hours. Thus, if the proposed amendments to Form N–CSR are adopted, the total annual hour burden for all funds for preparation and filing of Form N–CSR would be 111,000 hours.[46]

Shareholder Reports

Rule 30e–1, including the proposed amendments to Forms N–1A, N–2, and N–3, contains collection of information requirements.[47] Compliance with the disclosure requirements of rule 30e–1 is mandatory. Responses to the disclosure requirements will not be kept confidential.

There are approximately 3,700 management investment companies subject to rule 30e–1. We estimate that the current hour burden for preparing and filing semi-annual and annual shareholder reports in compliance with rule 30e–1 is 202.5 hours. We estimate that the proposed amendments would increase the hour burden of complying with rule 30e–1 by 10 hours. Thus, if the proposed amendments are adopted, the total hour burden of complying with rule 30e–1 would be 212.5 hours, for a total annual burden to the industry of 786,250 hours.

Request for Comments

We request your comments on the accuracy of our estimates. Pursuant to 44 U.S.C. 3506(c)(2)(B), the Commission solicits comments to: (i) Evaluate whether the proposed collection of information is necessary for the proper performance of the functions of the agency, including whether the information will have practical utility; (ii) evaluate the accuracy of the Commission's estimate of burden of the proposed collection of information; (iii) determine whether there are ways to enhance the quality, utility, and clarity of the information to be collected; and (iv) evaluate whether there are ways to minimize the burden of the collection of information on those who are to respond, including through the use of automated collection techniques or other forms of information technology.

Persons submitting comments on the collection of information requirements should direct the comments to the Office of Management and Budget, Attention: Desk Officer for the Securities and Exchange Commission, Office of Information and Regulatory Affairs, Room 3208, New Executive Office Building, Washington, DC 20503, and should send a copy to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 5th Street, NW, Washington, DC 20549–0609, with reference to File No. S7–36–02. OMB is required to make a decision concerning the collection of information between 30 and 60 days after publication of this release. Consequently, a comment to OMB is best assured of having its full effect if OMB receives it within 30 days after publication of this Release.

V. Cost/Benefit Analysis

The Commission is sensitive to the costs and benefits imposed by its rules. We propose to require funds to provide disclosure about how they vote proxies of the portfolio securities they hold. Funds would be required to disclose in their registration statements their policies and procedures used to determine how to vote proxies relating to portfolio securities, and to include disclosure about the availability of the fund's proxy voting record. This disclosure would be included in the statement of additional information (''SAI''), which is not part of the fund's prospectus but is delivered to investors free of charge upon request. We are also proposing to require a fund to file with the Commission semi-annually, as part of its reports on proposed Form N–CSR, its complete proxy voting record for the period covered by the report. Our proposals would also require a fund to include in its annual and semi-annual reports to shareholders disclosure that this record, and the fund's proxy voting policies and procedures, are available (i) without charge, upon request from the fund, (ii) on the fund's website, if applicable, and (iii) on the SEC website. Finally, our proposals would require disclosure in shareholder reports of any proxy votes that are inconsistent with the fund's policies and procedures.

A. Benefits

The proposed form amendments will benefit fund investors, by providing them with access to information about how funds vote their proxies. To the extent that investors would choose among funds based on their proxy voting policies and records, in addition to other factors such as expenses and investment policies, investors will be better able to select funds that suit their particular preferences.

In some situations the interests of a mutual fund's shareholders may conflict with those of its investment adviser with respect to proxy voting. This may occur, for example, when a fund's adviser also manages or seeks to manage the retirement plan assets of a company whose securities are held by the fund. In these situations, a fund's adviser may have an incentive to support management recommendations to further its business interests. Our proposals would require funds to disclose how they address such conflicts of interest in determining how to vote their proxies, and would also require funds to identify any proxy votes that are inconsistent with their stated voting policies. This disclosure requirement should benefit fund shareholders by deterring voting decisions that are motivated by considerations of the interests of the fund's adviser rather than the interests of fund shareholders.

Moreover, the proposed rules could increase funds' focus on corporate governance. This could result in better decisionmaking in particular corporate governance matters, which may enhance shareholder value of the issuers of portfolio securities, and may, in turn, benefit both investors in the fund and other investors in these issuers. These benefits are difficult to quantify. We note that assets held in equity funds account for approximately 19% of the market capitalization of all publicly

[45] *See* Investment Company Act Release No. 25723 (Aug. 30, 2002) [67 FR 57298 (Sept. 9, 2002)].

[46] This increase in hour burden includes that imposed by Item 3 of proposed Form N–CSR with respect to policies and procedures used by a closed-end fund in determining how to vote proxies relating to portfolio securities.

[47] The proposed amendments are to Forms N–1A, N–2, and N–3. Rule 30e–1(a) under the Investment Company Act of 1940 [17 CFR 270.30e–1(a)] requires funds to include in the shareholder reports the information that is required by the fund's registration statement form.

traded U.S. corporate equity.[48] We request comment on the extent and magnitude of the effect that requiring disclosure of proxy voting guidelines and decisions by funds would have on corporate governance, and on the U.S. economy generally.

B. Costs

The proposed amendments would lead to some additional costs for funds, which may be passed on to fund shareholders.

Our proposals would require new disclosure by a fund regarding its proxy voting policies and records, in its SAI and its annual and semi-annual reports to shareholders. These costs would include both internal costs (for attorneys and other non-legal staff of a fund, such as computer programmers, to prepare and review the required disclosure) and external costs (for printing and typesetting of the disclosure).[49] First, our proposals would require disclosure of the fund's proxy voting policies and procedures, and disclosure about the availability of its proxy voting record, in the fund's SAI. Because the SAI is typically not typeset and is only provided to shareholders upon request, we estimate that the external costs per investment company of this additional disclosure in the SAI would be minimal. For purposes of the Paperwork Reduction Act, we have estimated that the disclosure requirements would add 18,270 hours to the burden of completing Forms N–1A, N–2 and N–3.[50] We estimate that this additional burden would equal total internal costs of $1,259,534 annually, or $340 per investment company.[51]

Second, with respect to annual and semi-annual reports to shareholders, funds would be required to include disclosure about the availability of information regarding the fund's proxy voting policies and procedures, and proxy voting record, and to disclose any proxy votes that were inconsistent with the fund's proxy voting policies and procedures. We estimate that to comply with these disclosure requirements, a typical fund would need to include at most one additional page in its annual and semi-annual reports to shareholders, at a typesetting cost of $55 per page and a printing cost of $0.025 per page.[52] We estimate that a typical fund may have, on average, 30,000 shareholder accounts;[53] therefore, the additional disclosure in shareholder reports would cost approximately $1610 (($0.025 × 30,000 shareholder accounts, plus $55) × 2 reports per year) in external costs per fund. Based on the Commission's estimate of 3700 registered management investment companies, we estimate these external costs would be $5,957,000 for the industry as a whole. In addition, we estimate that these disclosure requirements would add 37,000 burden hours for management investment companies required to transmit shareholder reports, or 10 hours per fund, equal to internal costs of $2,550,780 for the industry annually, or $689 per investment company.[54]

Third, our proposals also would require funds to file with the Commission information regarding each matter relating to a portfolio security considered at any shareholder meeting held during the period covered by the report on proposed Form N–CSR, and to make available to their shareholders the information contained in proposed Form N–CSR. We estimate that the external costs per investment company of this additional disclosure would be minimal. In addition, we estimate that these disclosure requirements would add 74,000 burden hours to Form N–CSR, or 20 hours per management investment company filing on Form N–CSR annually. We estimate that this burden would be $5,101,560 in total internal costs annually, or $1,379 per investment company.[55]

Therefore, based on this analysis, we estimate that the total external and internal costs of the additional disclosure that would be required by the proposed amendments would be $14,868,874. We request comment on the nature and magnitude of our estimates of the costs of the additional disclosure that would be required if our proposals were adopted.

Because the proposed amendments may have the effect of inducing fund advisers and fund boards to devote more resources to articulating their proxy voting policies and procedures in more detail, and to monitoring proxy voting decisions, they may result in higher expenses and advisory fees for funds. Some of these expenses may be passed on to shareholders. We request comment on the extent to which the proposed amendments would increase costs to funds and their shareholders as well as affect shareholder value.

C. Request for Comments

We request comments on all aspects of this cost-benefit analysis, including identification of any additional costs or benefits of, or suggested alternatives to, the proposed amendments. Commenters are requested to provide empirical data and other factual support for their views to the extent possible.

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.[56] In addition, section 2(c) of the Investment Company Act, section 2(b) of the Securities Act, and section 3(f) of the Exchange Act 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.[57]

[48] *See* Securities Industry Fact Book, *supra* note 5, at 71.

[49] Based on the Division's review of materials submitted by various mutual fund complexes, we believe that most registered management investment companies currently maintain policies and procedures used to determine how to vote proxies relating to portfolio securities.

[50] This would represent 16,594 additional hours for Form N–1A, 1,196 additional hours for Form N–2, and 480 additional hours for Form N–3.

[51] These figures are based on a Commission estimate that approximately 3,700 management investment companies would be subject to the proposed amendments and an estimated hourly wage rate of $68.94. The estimate of the number of investment companies is based on data derived from the Commission's EDGAR filing system. The estimated wage rate figure is based on published hourly wage rates for compliance attorneys in New York City ($74.22) and programmers ($27.91), and the estimate, based on the Commission staff's discussions with certain fund complexes, that attorneys and programmers would divide time equally on compliance with the proxy voting disclosure requirements, yielding a weighted wage rate of $51.065 (($74.22 × .50) + (27.91 × .50)) = $51.065). *See* Securities Industry Association, *Report on Management & Professional Earnings in the Securities Industry 2001* (Oct. 2001). This weighted wage rate was then adjusted upward by 35% for overhead, reflecting the costs of supervision, space, and administrative support, to obtain the total per hour internal cost of $68.94 (51.065 × 1.35) = $68.94.

[52] This estimate is based on information provided to the Division of Investment Management by registered investment companies regarding printing and typesetting costs for prospectuses and SAIs.

[53] This estimate regarding the average number of shareholder accounts per typical fund is derived from data provided in the Mutual Fund Fact Book, *supra* note 5, at 63, 64.

[54] These figures are based on a Commission estimate that approximately 3,700 investment companies would be subject to the proposed amendments and an estimated hourly wage rate of $68.94. *See supra* note.

[55] *Id.*

[56] 15 U.S.C. 78w(a)(2).

[57] 15 U.S.C. 77(b), 78c(f), and 80a–2(c).

The proposed amendments are intended to provide greater transparency for fund shareholders regarding the management of their investments in funds. The changes may improve efficiency. The enhanced disclosure requirements would provide shareholders with greater access to proxy voting policies and decisions of the funds in which they invest, which would promote more efficient allocation of investments by investors and more efficient allocation of assets among competing funds. The proposed amendments may also improve competition, as enhanced disclosure may prompt funds to seek to provide better-informed investors with improved products and services. Finally, the effects of the proposed amendments on capital formation are unclear. Although, as noted above, we believe that the proposed amendments would benefit investors, the magnitude of the effect of the proposed amendments on efficiency, competition, and capital formation is difficult to quantify, particularly given that most funds do not currently provide the type of disclosure contemplated by the proposed amendments.

We request comment on whether the proposed amendments, if adopted, would impose a burden on competition. We also request comment on whether the proposed amendments, if adopted, would promote efficiency, competition, and capital formation. Commenters are requested to provide empirical data and other factual support for their views if possible.

VII. Initial Regulatory Flexibility Analysis

This Initial Regulatory Flexibility Analysis (''Analysis'') has been prepared in accordance with 5 U.S.C. 603, and relates to the Commission's proposed form amendments under the Securities Act, the Exchange Act, and the Investment Company Act to require funds to provide disclosure about how they vote proxies of portfolio securities they hold. Under the proposed amendments, funds would be required to disclose in their registration statements the policies and procedures that they use to determine how to vote the proxies of portfolio securities. The proposal also would require funds to file with the Commission and to make available to their shareholders, upon request and without charge, a document containing the information required by proposed Form N–CSR.

Specifically, a fund would be required to disclose in its statement of additional information (''SAI'') its policies and procedures used to determine how to vote proxies of the securities held in its portfolio, and to provide disclosure regarding the availability of its proxy voting record to shareholders. The proposals also would require a fund to file with the Commission, as part of its reports on proposed Form N–CSR, its complete proxy voting record for the period covered by the report. Finally, the proposals also would require a fund to include in its annual and semi-annual reports to shareholders disclosure that this record, and the fund's proxy voting policies and procedures, are available (i) without charge, upon request from the fund, (ii) on the fund's Web site, if applicable, and (iii) on the SEC Web site, and to include disclosure about any proxy votes cast by the fund that are inconsistent with its policies and procedures.

A. Reasons for, and Objectives of, Proposed Amendments

As we have noted above, proxy voting decisions may play an important role in maximizing the value of a fund's investments for its shareholders. Requiring funds to disclose specific proxy voting information could enable shareholders to make an informed assessment as to whether funds are utilizing proxy voting for the benefit of fund shareholders. We are proposing these amendments because we believe that requiring management investment companies to disclose their proxy policies and procedures as well as voting records will result in greater transparency for fund shareholders regarding the overall management of their investments. We also believe it is possible to achieve this improved disclosure quickly and inexpensively because of the advancements in technology over the last 30 years, such as the Internet.

B. Legal Basis

The Commission is proposing amendments to Forms N–1A, N–2, N–3, and N–CSR pursuant to authority set forth in sections 5, 6, 7, 10, 19(a), and 28 of the Securities Act [15 U.S.C. 77e, 77f, 77g, 77j, 77s(a), and 77z–3], 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], and 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].

C. Small Entities Subject to the Rule

For purposes of the Regulatory Flexibility Act, 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.[58] Approximately 205 out of 3700 investment companies that would be affected by this rule meet this definition.[59]

D. Reporting, Recordkeeping, and Other Compliance Requirements

The proposed amendments would require a fund to disclose in its SAI its policies and procedures used to determine how to vote proxies for the securities held in its portfolio, and to provide disclosure regarding the availability of its proxy voting record to shareholders. The proposals would also require a fund to file with the Commission, as part of its reports on proposed Form N–CSR, its complete proxy voting record for the period covered by the report. Finally, the proposals would require a fund to include in its annual and semi-annual reports to shareholders disclosure that this proxy voting record, and the fund's proxy voting policies and procedures, are available (i) without charge, upon request, from the fund, (ii) on the fund's Web site, if applicable, and (iii) on the SEC Web site, and to include disclosure about any proxy votes cast by the fund that are inconsistent with its policies and procedures.

The Commission estimates some one-time formatting and ongoing costs and burdens that would be imposed on all funds, but which may have a relatively greater impact on smaller firms. These include the costs related to disclosing proxy voting policies and procedures to fund shareholders; filing proxy voting records with the Commission on proposed Form N–CSR; and disclosing voting records via the Internet, U.S. mail, or other means. These costs also could include expenses for computer time, legal and accounting fees, information technology staff, and additional computer and telephone equipment. However, we believe, based on consultations with a number of fund complexes, including smaller fund complexes, that many investment companies presently collect in-house or outsource proxy voting information on a basis at least as current as semi-annually

[58] 17 CFR 270.0–10.

[59] This estimate is based on figures compiled by Division of Investment Management 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)]. Currently, no insurance company separate account filing on Form N–3 qualifies as a small entity.

and, therefore, that the marginal cost increases for most funds would be minimal.

The Commission solicits comment on the effect the proposed amendments would have on small entities.

E. Duplicative, Overlapping or Conflicting Federal Rules

There are no rules that duplicate, overlap, or conflict with the proposed amendments.

F. Significant Alternatives

The Regulatory Flexibility Act directs us to consider significant alternatives that would accomplish our stated objective, while minimizing any significant adverse impact on small issuers. In connection with the proposed amendments, the Commission considered the following alternatives: (i) The establishment of differing compliance or reporting requirements or timetables 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; (iii) the use of performance rather than design standards; and (iv) an exemption from coverage of the proposed amendments, or any part thereof, for small entities.

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 proposed disclosure amendments would provide shareholders with greater transparency regarding a fund's proxy voting policies and procedures, as well as records of votes cast. Different disclosure requirements for small entities, such as reducing the level of proxy voting disclosure that small entities would have to provide shareholders, may create the risk that those shareholders would not receive sufficient information to make an informed evaluation as to whether the fund's board and its investment adviser are complying with their fiduciary duties to vote proxies of portfolio securities in the best interest of fund shareholders. We believe it is important for the proxy disclosure that would be required by the proposed amendments to be provided to shareholders by all funds, not just funds that are not considered small entities.

We have endeavored through the proposed amendments to minimize the regulatory burden on all funds, including small entities, while meeting our regulatory objectives. Small entities should benefit from the Commission's reasoned approach to the proposed amendments to the same degree as other investment companies. Further clarification, consolidation, or simplification of the proposals for funds that are small entities would be inconsistent with the Commission's concern for investor protection. Finally, we do not consider using performance rather than design standards to be consistent with our statutory mandate of investor protection in the present context.

G. Solicitation of Comments

The Commission encourages the submission of written comments with respect to any aspect of this analysis. Comment is specifically requested on the number of small entities that would be affected by the proposed amendments and the likely impact of the proposals on small entities. Commenters are asked to describe the nature of any impact and provide empirical data supporting the extent of the impact. These comments will be considered in the preparation of the Final Regulatory Flexibility Analysis, if the proposed amendments are adopted, and will be placed in the same public file as comments on the proposed amendments themselves. Comments should be submitted in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549–0609. Comments also may be submitted electronically at the following e-mail address: *rule-comments@sec.gov.* All comment letters should refer to File No. S7–36–02; this file number should be included on the subject line if e-mail is used. Comment letters will be available for public inspection and copying in the Commission's Public Reference Room, 450 Fifth Street, NW., Washington, DC 20549–0102. Electronically submitted comment letters also will be posted on the Commission's Internet Web site (*http://www.sec.gov*).[60]

VIII. Consideration of Impact on the Economy

For purposes of the Small Business Enforcement Fairness Act of 1996,[61] a rule is ''major'' if it results or is likely to result in:

- an annual effect on the economy of $100 million or more;
- a major increase in costs or prices for consumers or individual industries; or
- significant adverse effects on competition, investment, or innovation.

The Commission requests comment on the potential impact of the proposed amendments on the U.S. economy on an annual basis. Commenters are requested to provide empirical data to support their views.

IX. Statutory Authority

The Commission is proposing amendments to Forms N–1A, N–2, N–3, and proposed Form N–CSR pursuant to authority set forth in sections 5, 6, 7, 10, 19(a), and 28 of the Securities Act [15 U.S.C. 77e, 77f, 77g, 77j, 77s(a), and 77z–3], 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], and 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].

List of Subjects

17 CFR Parts 239 and 249

Reporting and recordkeeping requirements, Securities.

17 CFR Part 274

Investment companies, Reporting and recordkeeping requirements, Securities.

Text of Proposed Rule and Form Amendments

For the reasons set out in the preamble, the Commission proposes to amend title 17, chapter II of the Code of Federal Regulations as follows:

PART 239—FORMS PRESCRIBED UNDER THE SECURITIES ACT OF 1933

1. The authority citation for part 239 continues to read in part as follows:

Authority: 15 U.S.C. 77f, 77g, 77h, 77j, 77s, 77z–2, 77sss, 78c, 78*l*, 78m, 78n, 78o(d), 78u–5, 78w(a), 78*ll*(d), 79e, 79f, 79g, 79j, 79*l*, 79m, 79n, 79q, 79t, 80a–8, 80a–24, 80a–26, 80a–29, 80a–30, and 80a–37, unless otherwise noted.

* * * * *

PART 249—FORMS, SECURITIES EXCHANGE ACT OF 1934

2. The authority citation for part 249 continues to read in part as follows:

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

* * * * *

[60] We do not edit personal identifying information, such as names or electronic mail addresses, from electronic submissions. You should submit only information that you wish to make available publicly.

[61] Pub. L. 104–21, Title II, 110 Stat. 857 (1996).

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

3. The authority citation for part 274 is amended by adding the following citations to read as follows:

Authority: 15 U.S.C. 77f, 77g, 77h, 77j, 77s, 78c(b), 78*l*, 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) and 302, Pub. L. 107–204, 116 Stat. 745.

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

4. Form N–1A (referenced in §§ 239.15A and 274.11A) is amended by:

a. In Item 13, adding paragraph (f); and

b. In Item 22, adding paragraphs (b)(7) and (8) and (c)(5) and (6).

These amendments read as follows:

Note: The text of Form N–1A does not, and these amendments will not, appear in the *Code of Federal Regulations.*

Form N–1A

* * * * *

Item 13. Management of the Fund

* * * * *

(f) *Proxy Voting Policies.* Unless the Fund invests exclusively in non-voting securities, describe the policies and procedures that the Fund uses to determine how to vote proxies relating to portfolio securities, including the procedures that the Fund uses when a vote presents a conflict between the interests of Fund shareholders, on the one hand, and those of the Fund's investment adviser; principal underwriter; or any affiliated person of the Fund, its investment adviser, or its principal underwriter, on the other. Include any policies and procedures of the Fund's investment adviser, or any other third party, that the Fund uses, or that are used on the Fund's behalf, to determine how to vote proxies relating to portfolio securities. Also, state that shareholders may obtain information regarding how the Fund voted proxies relating to portfolio securities (1) without charge, upon request, by calling a specified toll-free (or collect) telephone number; (2) on the Fund's website, if applicable; and (3) on the Commission's Web site at *http://www.sec.gov.*

Instruction. When a Fund (or financial intermediary through which shares of the Fund may be purchased or sold) receives a request for information regarding how the Fund voted proxies relating to portfolio securities, the Fund (or financial intermediary) must send the information disclosed in response to Item 2 in the Fund's most recently filed Form N–CSR within 3 business days of receipt of the request by first-class mail or other means designed to ensure equally prompt delivery.

* * * * *

Item 22. Financial Statements

* * * * *

(b) * * *

(7) A statement that the Fund's proxy voting record for the period covered by the report, and a description of the policies and procedures that the Fund uses to determine how to vote proxies relating to portfolio securities, are available (i) without charge, upon request, by calling a specified toll-free (or collect) telephone number; (ii) on the Fund's Web site, if applicable; and (iii) on the Commission's Web site at *http://www.sec.gov.*

Instruction. When a Fund (or financial intermediary through which shares of the Fund may be purchased or sold) receives a request for the Fund's proxy voting record, or a request for a description of the policies and procedures that the Fund uses to determine how to vote proxies, the Fund (or financial intermediary) must send the information disclosed in response to Item 2 in the Fund's most recently filed Form N–CSR, in the case of a request for the Fund's proxy voting record, or the information disclosed in response to Item 13(f) of this Form, in the case of a request for a description of the Fund's policies and procedures, within 3 business days of receipt of the request by first-class mail or other means designed to ensure equally prompt delivery.

(8) In the case of each matter relating to a portfolio security considered at any shareholder meeting held during the period covered by the report and with respect to which the Fund was entitled to vote and voted (or failed to vote) in a manner that was inconsistent with the Fund's proxy voting policies and procedures disclosed pursuant to Item 13(f), the following information:

(i) The name of the issuer of the portfolio security;

(ii) The exchange ticker symbol of the portfolio security;

(iii) The Council on Uniform Securities Identification Procedures (''CUSIP'') number for the portfolio security;

(iv) The shareholder meeting date;

(v) A brief identification of the matter voted on;

(vi) Whether the matter was proposed by the issuer or by a security holder;

(vii) Whether the Fund cast its vote on the matter;

(viii) How the Fund cast its vote (*e.g.*, for or against proposal, or abstain; for or withhold regarding election of directors);

(ix) Whether the Fund cast its vote for or against management; and

(x) The reasons why the Fund voted, or failed to vote, in a manner that was inconsistent with its proxy voting policies and procedures.

(c) * * *

(5) A statement that the Fund's proxy voting record for the period covered by the report, and a description of the policies and procedures that the Fund uses to determine how to vote proxies relating to portfolio securities, are available (i) without charge, upon request, by calling a specified toll-free (or collect) telephone number; (ii) on the Fund's Web site, if applicable; and (iii) on the Commission's Web site at *http://www.sec.gov.*

Instruction. When a Fund (or financial intermediary through which shares of the Fund may be purchased or sold) receives a request for the Fund's proxy voting record, or a request for a description of the policies and procedures that the Fund uses to determine how to vote proxies, the Fund (or financial intermediary) must send the information disclosed in response to Item 2 in the Fund's most recently filed Form N–CSR, in the case of a request for the Fund's proxy voting record, or the information disclosed in response to Item 13(f) of this Form, in the case of a request for a description of the Fund's policies and procedures, within 3 business days of receipt of the request by first-class mail or other means designed to ensure equally prompt delivery.

(6) In the case of each matter relating to a portfolio security considered at any shareholder meeting held during the period covered by the report and with respect to which the Fund was entitled to vote and voted (or failed to vote) in a manner that was inconsistent with the Fund's proxy voting policies and procedures disclosed pursuant to Item 13(f), the following information:

(i) The name of the issuer of the portfolio security;

(ii) The exchange ticker symbol of the portfolio security;

(iii) The Council on Uniform Securities Identification Procedures (''CUSIP'') number for the portfolio security;

(iv) The shareholder meeting date;

(v) A brief identification of the matter voted on;

(vi) Whether the matter was proposed by the issuer or by a security holder;

(vii) Whether the Fund cast its vote on the matter;

(viii) How the Fund cast its vote (*e.g.*, for or against proposal, or abstain; for or withhold regarding election of directors);

(ix) Whether the Fund cast its vote for or against management; and

(x) The reasons why the Fund voted, or failed to vote, in a manner that was inconsistent with its proxy voting policies and procedures.

* * * * *

5. Form N–2 (referenced in §§ 239.14 and 274.11a–1) is amended by:

a. In Item 18, adding paragraph 16;

b. In Item 23, removing ''and'' from the end of Instruction 4.e.;

c. In Item 23, removing the period from the end of Instruction 4.f. and in its place adding a semi-colon;

d. In Item 23, adding Instructions 4.g. and 4.h.;

e. In Item 23, removing ''and'' from the end of Instruction 5.c.;

f. In Item 23, removing the period from the end of Instruction 5.d. and in its place adding a semi-colon;

g. In Item 23, adding Instructions 5.e. and 5.f.;

h. In Item 23, redesignating Instruction 6 as Instruction 7; and

i. In Item 23, adding new Instruction 6.

These amendments read as follows:

Note: The text of Form N–2 does not, and these amendments will not, appear in the *Code of Federal Regulations.*

Form N–2

* * * * *

Item 18. Management

* * * * *

16. Unless the Registrant invests exclusively in non-voting securities, describe the policies and procedures that the Registrant uses to determine how to vote proxies relating to portfolio securities, including the procedures that the Registrant uses when a vote presents a conflict between the interests of the Registrant's shareholders, on the one hand, and those of the Registrant's investment adviser; principal underwriter; or any affiliated person (as defined in section 2(a)(3) of the 1940 Act (15 U.S.C. 80a–2(a)(3)) and the rules thereunder) of the Registrant, its investment adviser, or its principal underwriter, on the other. Include any policies and procedures of the Registrant's investment adviser, or any other third party, that the Registrant uses, or that are used on the Registrant's behalf, to determine how to vote proxies relating to portfolio securities. Also, state that shareholders may obtain information regarding how the Registrant voted proxies relating to portfolio securities (i) without charge, upon request, by calling a specified toll-free (or collect) telephone number; (ii) on the Registrant's Web site, if applicable; and (iii) on the Commission's Web site at *http://www.sec.gov.*

Instruction. When a Registrant (or financial intermediary through which shares of the Registrant may be purchased or sold) receives a request for information regarding how the Registrant voted proxies relating to portfolio securities, the Registrant (or financial intermediary) must send the information disclosed in response to Item 2 in the Registrant's most recently filed Form N–CSR within 3 business days of receipt of the request by first-class mail or other means designed to ensure equally prompt delivery.

* * * * *

Item 23. Financial Statements

* * * * *

Instructions:

* * * * *

4. * * *

g. a statement that the Registrant's proxy voting record for the period covered by the report, and a description of the policies and procedures that the Registrant uses to determine how to vote proxies relating to portfolio securities, are available (1) without charge, upon request, by calling a specified toll-free (or collect) telephone number; (2) on the Registrant's Web site, if applicable; and (3) on the Commission's Web site at *http://www.sec.gov;* and

h. in the case of each matter relating to a portfolio security considered at any shareholder meeting held during the period covered by the report and with respect to which the Registrant was entitled to vote and voted (or failed to vote) in a manner that was inconsistent with the Registrant's proxy voting policies and procedures most recently disclosed pursuant to Item 18.16 of this Form or Item 3 of Form N–CSR, the following information:

(1) the name of the issuer of the portfolio security;

(2) the exchange ticker symbol of the portfolio security;

(3) the Council on Uniform Securities Identification Procedures (''CUSIP'') number for the portfolio security;

(4) the shareholder meeting date;

(5) a brief identification of the matter voted on;

(6) whether the matter was proposed by the issuer or by a security holder;

(7) whether the Registrant cast its vote on the matter;

(8) how the Registrant cast its vote (*e.g.*, for or against proposal, or abstain; for or withhold regarding election of directors);

(9) whether the Registrant cast its vote for or against management; and

(10) the reasons why the Registrant voted, or failed to vote, in a manner that was inconsistent with its proxy voting policies and procedures.

5. * * *

e. a statement that the Registrant's proxy voting record for the period covered by the report, and a description of the policies and procedures that the Registrant uses to determine how to vote proxies relating to portfolio securities, are available (1) without charge, upon request, by calling a specified toll-free (or collect) telephone number; (2) on the Registrant's Web site, if applicable; and (3) on the Commission's Web site at *http://www.sec.gov;* and

f. in the case of each matter relating to a portfolio security considered at any shareholder meeting held during the period covered by the report and with respect to which the Registrant was entitled to vote and voted (or failed to vote) in a manner that was inconsistent with the Registrant's proxy voting policies and procedures most recently disclosed pursuant to Item 18.16 of this Form or Item 3 of Form N–CSR, the following information:

(1) the name of the issuer of the portfolio security;

(2) the exchange ticker symbol of the portfolio security;

(3) the Council on Uniform Securities Identification Procedures (''CUSIP'') number for the portfolio security;

(4) the shareholder meeting date;

(5) a brief identification of the matter voted on;

(6) whether the matter was proposed by the issuer or by a security holder;

(7) whether the Registrant cast its vote on the matter;

(8) how the Registrant cast its vote (*e.g.*, for or against proposal, or abstain; for or withhold regarding election of directors);

(9) whether the Registrant cast its vote for or against management; and

(10) the reasons why the Registrant voted, or failed to vote, in a manner that was inconsistent with its proxy voting policies and procedures.

6. When a Registrant (or financial intermediary through which shares of the Registrant may be purchased or sold) receives a request for the Registrant's proxy voting record, or a request for a description of the policies and procedures that the Registrant uses to determine how to vote proxies, the Registrant (or financial intermediary) must send the information disclosed in response to Item 2 in the Registrant's most recently filed Form N–CSR, in the

case of a request for the Registrant's proxy voting record, or the information most recently disclosed in response to Item 18.16 of this Form or Item 3 of Form N–CSR, in the case of a request for a description of the Registrant's policies and procedures, within 3 business days of receipt of the request by first-class mail or other means designed to ensure equally prompt delivery.

* * * * *

6. Form N–3 (referenced in §§ 239.17 and 274.11b) is amended by:

a. In Item 20, adding paragraph (o);

b. In Item 27(a), removing ''and'' from the end of Instruction 4(v);

c. In Item 27(a), removing the period from the end of Instruction 4(vi) and in its place adding a semi-colon;

d. In Item 27(a), adding Instructions 4(vii) and 4(viii);

e. In Item 27(a), removing ''and'' from the end of Instruction 5(iii);

f. In Item 27(a), removing the period from the end of Instruction 5(iv) and in its place adding a semi-colon;

g. In Item 27(a), adding Instructions 5(v) and 5(vi);

h. In Item 27(a), redesignating Instruction 6 as Instruction 7; and

i. In Item 27(a), adding new Instruction 6.

These amendments read as follows:

Note: The text of Form N–3 does not, and these amendments will not, appear in the Code of Federal Regulations.

Form N–3

* * * * *

Item 20. Management

* * * * *

(o) Unless the Registrant invests exclusively in non-voting securities, describe the policies and procedures that the Registrant uses to determine how to vote proxies relating to portfolio securities, including the procedures that the Registrant uses when a vote presents a conflict between the interests of the Registrant's contractowners, on the one hand, and those of the Registrant's investment adviser; principal underwriter; or any affiliated person (as defined in Section 2(a)(3) of the 1940 Act (15 U.S.C. 80a–2(a)(3)) and the rules thereunder) of the Registrant, its investment adviser, or its principal underwriter, on the other. Include any policies and procedures of the Registrant's investment adviser, or any other third party, that the Registrant uses, or that are used on the Registrant's behalf, to determine how to vote proxies relating to portfolio securities. Also, state that contractowners may obtain information regarding how the Registrant voted proxies relating to portfolio securities (i) without charge, upon request, by calling a specified toll-free (or collect) telephone number; (ii) on the Registrant's Web site, if applicable; and (iii) on the Commission's Web site at *http://www.sec.gov.*

Instruction. When a Registrant (or financial intermediary through which shares of the Registrant may be purchased or sold) receives a request for information regarding how the Registrant voted proxies relating to portfolio securities, the Registrant (or financial intermediary) must send the information disclosed in response to Item 2 in the Registrant's most recently filed Form N–CSR within 3 business days of receipt of the request by first-class mail or other means designed to ensure equally prompt delivery.

* * * * *

Item 27. Financial Statements

(a) * * *

Instructions:

* * * * *

4. * * *

(vii) a statement that the Registrant's proxy voting record for the period covered by the report, and a description of the policies and procedures that the Registrant uses to determine how to vote proxies relating to portfolio securities, are available (A) without charge, upon request, by calling a specified toll-free (or collect) telephone number; (B) on the Registrant's Web site, if applicable; and (C) on the Commission's Web site at *http://www.sec.gov;* and

(viii) in the case of each matter relating to a portfolio security considered at any shareholder meeting held during the period covered by the report and with respect to which the Registrant was entitled to vote and voted (or failed to vote) in a manner that was inconsistent with the Registrant's proxy voting policies and procedures disclosed pursuant to Item 20(o), the following information:

(A) the name of the issuer of the portfolio security;

(B) the exchange ticker symbol of the portfolio security;

(C) the Council on Uniform Securities Identification Procedures (''CUSIP'') number for the portfolio security;

(D) the shareholder meeting date;

(E) a brief identification of the matter voted on;

(F) whether the matter was proposed by the issuer or by a security holder;

(G) whether the Registrant cast its vote on the matter;

(H) how the Registrant cast its vote (*e.g.*, for or against proposal, or abstain; for or withhold regarding election of directors);

(I) whether the Registrant cast its vote for or against management; and

(J) the reasons why the Registrant voted, or failed to vote, in a manner that was inconsistent with its proxy voting policies and procedures.

5. * * *

(v) a statement that the Registrant's proxy voting record for the period covered by the report, and a description of the policies and procedures that the Registrant uses to determine how to vote proxies relating to portfolio securities, are available (A) without charge, upon request, by calling a specified toll-free (or collect) telephone number; (B) on the Registrant's Web site, if applicable; and (C) on the Commission's Web site at *http://www.sec.gov;* and

(vi) in the case of each matter relating to a portfolio security considered at any shareholder meeting held during the period covered by the report and with respect to which the Registrant was entitled to vote and voted (or failed to vote) in a manner that was inconsistent with the Registrant's proxy voting policies and procedures disclosed pursuant to Item 20(o), the following information:

(A) the name of the issuer of the portfolio security;

(B) the exchange ticker symbol of the portfolio security;

(C) the Council on Uniform Securities Identification Procedures (''CUSIP'') number for the portfolio security;

(D) the shareholder meeting date;

(E) a brief identification of the matter voted on;

(F) whether the matter was proposed by the issuer or by a security holder;

(G) whether the Registrant cast its vote on the matter;

(H) how the Registrant cast its vote (*e.g.*, for or against proposal, or abstain; for or withhold regarding election of directors);

(I) whether the Registrant cast its vote for or against management; and

(J) the reasons why the Registrant voted, or failed to vote, in a manner that was inconsistent with its proxy voting policies and procedures.

6. When a Registrant (or financial intermediary through which shares of the Registrant may be purchased or sold) receives a request for the Registrant's proxy voting record, or a request for a description of the policies and procedures that the Registrant uses to determine how to vote proxies, the Registrant (or financial intermediary) must send the information disclosed in response to Item 2 in the Registrant's most recently filed Form N–CSR, in the case of a request for the Registrant's proxy voting record, or the information disclosed in response to Item 20(o) of

this Form, in the case of a request for a description of the Registrant's policies and procedures, within 3 business days of receipt of the request by first-class mail or other means designed to ensure equally prompt delivery.

* * * * *

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

7. Form N–CSR (referenced in §§ 249.331 and 274.128; as proposed in 67 FR 57298 (9/9/02)) is amended by:

a. Redesignating Item 2 as Item 4; and

b. Adding new Items 2 and 3 to read as follows:

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

Form N–CSR

* * * * *

Item 2. Proxy Voting Records.

Disclose the following information for each matter relating to a portfolio security considered at any shareholder meeting held during the period covered by the report provided pursuant to Item 1 and with respect to which the registrant was entitled to vote:

(1) The name of the issuer of the portfolio security;

(2) The exchange ticker symbol of the portfolio security;

(3) The Council on Uniform Securities Identification Procedures (''CUSIP'') number for the portfolio security;

(4) The shareholder meeting date;

(5) A brief identification of the matter voted on;

(6) Whether the matter was proposed by the issuer or by a security holder;

(7) Whether the registrant cast its vote on the matter;

(8) How the registrant cast its vote (*e.g.*, for or against proposal, or abstain; for or withhold regarding election of directors); and

(9) Whether the registrant cast its vote for or against management.

Instruction. In the case of a registrant that offers multiple series of shares, provide the information required by this Item separately for each series. The term ''series'' means shares offered by a registrant that represent undivided interests in a portfolio of investments and that are preferred over all other series of shares for assets specifically allocated to that series in accordance with Rule 18f–2(a) under the Investment Company Act of 1940 (17 CFR 270.18f–2(a)).

Item 3. Disclosure of Proxy Voting Policies and Procedures for Closed-End Management Investment Companies

A closed-end management investment company that, pursuant to Item 1, is including a copy of an annual report transmitted to stockholders must, unless it invests exclusively in non-voting securities, describe the policies and procedures that it uses to determine how to vote proxies relating to portfolio securities, including the procedures that the company uses when a vote presents a conflict between the interests of its shareholders, on the one hand, and those of the company's investment adviser; principal underwriter; or any affiliated person (as defined in section 2(a)(3) of the Investment Company Act of 1940 (15 U.S.C. 80a–2(a)(3)) and the rules thereunder) of the company, its investment adviser, or its principal underwriter, on the other. Include any policies and procedures of the company's investment adviser, or any other third party, that the company uses, or that are used on the company's behalf, to determine how to vote proxies relating to portfolio securities.

* * * * *

By the Commission.

Dated: September 20, 2002.

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 02–24409 Filed 9–25–02; 8:45 am]

BILLING CODE 8010–01–P

SECURITIES AND EXCHANGE COMMISSION

17 CFR Part 275

[Release No. IA–2059; File No. S7–38–02]

RIN 3235–AI65

Proxy Voting By Investment Advisers

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rule.

SUMMARY: The Commission is publishing for comment a new rule and rule amendments under the Investment Advisers Act of 1940 that would address an investment adviser's fiduciary obligation to clients who have given the adviser authority to vote their proxies. Under our proposal, an investment adviser that exercises voting authority over client proxies would be required to adopt and implement policies and procedures that are reasonably designed to ensure that the adviser votes proxies in the best interest of clients, disclose to clients information about those procedures and policies and how clients may obtain information on how the adviser has voted their proxies, and retain certain records relating to proxy voting. The rule and rule amendments are designed to assure that advisers vote proxies in the best interest of their clients and provide clients with information about how their proxies are voted.

DATES: Comments must be received on or before December 6, 2002.

ADDRESSES: To help us process and review your comments more efficiently, comments should be sent by hard copy or e-mail, but not by both methods.

Comments sent by hardcopy should be submitted in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549–0609. Comments may also be submitted electronically at the following e-mail address: *rule-comments@sec.gov.* All comment letters should refer to File No. S7–38–02; if e-mail is used, this file number should be included on the subject line. Comment letters will be available for public inspection and copying in the Commission's Public Reference Room, 450 Fifth Street, NW., Washington, DC 20549. Electronically submitted comment letters also will be posted on the Commission's Internet Web site (*http://www.sec.gov*).[1]

FOR FURTHER INFORMATION CONTACT: Daniel S. Kahl, Senior Counsel, or Jamey Basham, Special Counsel, at 202–942–0719, Office of Investment Adviser Regulation, Division of Investment Management, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549–0506.

SUPPLEMENTARY INFORMATION: The Securities and Exchange Commission (''Commission'' or ''SEC'') is requesting public comment on proposed rule 206(4)–6 [17 CFR 275.206(4)–6] and proposed amendments to rule 204–2 [17 CFR 275.204–2] under the Investment Advisers Act of 1940 [15 U.S.C. 80b] (''Advisers Act'' or ''Act'').

I. Background

Investment advisers today have discretionary investment authority with respect to almost $19 trillion dollars of assets, including large holdings in equity securities.[2] In most cases, these

[1] We do not edit personal or identifying information, such as names or E-mail addresses, from electronic submissions. Submit only information you wish to make publicly available.

[2] Approximately $7 trillion of these assets are held by mutual funds. In a companion release, we are also publishing proposed amendments that would require mutual funds to disclose policies and procedures they use to vote proxies on their portfolio securities, and to make available to their

Continued