

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

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

In October 2002, we proposed amendments to proposed Form N-CSR and Form N-SAR to implement Sections 406 and 407 of the Sarbanes-Oxley Act with respect to registered investment companies, similar to disclosure requirements that we proposed at the same time with respect to operating companies.⁷ Section 406

directs the Commission to adopt rules requiring an issuer to disclose whether or not it has adopted a code of ethics for the issuer's senior financial officers, as well as any change to, or waiver of, that code of ethics. Section 407 directs the Commission to adopt rules: (1) Requiring an issuer to disclose whether or not its audit committee includes at least one member who is a financial expert; and (2) defining the term "financial expert." Earlier this month, we adopted disclosure requirements to implement these provisions with respect to operating companies.⁸ Today, we adopt similar disclosure requirements for registered management investment companies.

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

II. Discussion

The Commission today is adopting new rules, rule and form amendments, and new Form N-CSR under the Investment Company Act to better implement the certification requirement of Section 302 of the Sarbanes-Oxley Act for registered management investment companies, with modifications to address commenters' concerns.¹¹ Our amendments will

require a registered management investment company to file semi-annual reports on Form N-CSR, and will require the certification specified by Section 302 of the Sarbanes-Oxley Act in these semi-annual reports. Further, our amendments will remove the certification requirement from Form N-SAR, with respect to all registered investment companies.¹² In addition, we are adopting rules to require registered management investment companies to maintain, and regularly evaluate the effectiveness of, controls and procedures designed to ensure that the information required in reports on Form N-CSR is recorded, processed, summarized, and reported on a timely basis. Finally, we are adopting amendments to Form N-CSR and Form N-SAR to implement Sections 406 and 407 of the Sarbanes-Oxley Act with respect to registered management investment companies, similar to amendments that we adopted earlier this month to implement these provisions with respect to operating companies.

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

1. Certified Shareholder Reports

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

commenters included 12 mutual funds and investment advisers; one trade association; four law firms, bar associations, and accounting firms; and six independent directors of investment companies. These comment letters are available for public inspection and copying in our Public Reference Room, 450 Fifth Street, NW., Washington, DC 20549, in File No. S7-40-02. Public comments submitted electronically are available on our Web site <<http://www.sec.gov>>.

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

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

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

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

⁶ Form N-CSR Proposing Release, *supra* note 5, 67 FR at 57299.

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

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

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

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

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

We received over 200 comment letters on the Section 406/407 Proposing Release, including 23 comment letters on the proposed amendments applicable to investment companies. The