

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

We are not persuaded by these comments. Section 302 of the Sarbanes-Oxley Act does not limit the scope of the certification to financial information filed by a registrant. The MDPF and other narrative disclosure is relied upon by investors to explain the investment operations and performance of a mutual fund, which is as significant for investors in the fund as management's discussion and analysis of financial condition and results of operations is for investors in an operating company. In its integrated reviews of mutual fund prospectuses and shareholder reports, the staff has identified instances where MDPF has provided insufficient substantive discussion of the factors that affected the fund's performance during

the most recent fiscal year.²⁹ The Commission has asked the staff, in its review of a mutual fund's disclosure documents, to continue to focus on areas where funds' MDPF disclosure has been deficient.³⁰ We believe that a requirement that MDPF, if included in shareholder reports, must be certified by the mutual fund's principal executive and financial officers, would encourage funds to include a more complete and accurate discussion of the factors that affected fund performance in their MDPF. Further, we note that in the operating company context, reports on Form 10-K contain certain required non-financial information that must be certified.³¹

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

under the Exchange Act meet this standard.

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

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

³⁴ Instruction 102P3 of Form N-SAR; Instruction to Item 133 of Form N-SAR.

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

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

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

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

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

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

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

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

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