

provided that, where requested, the company would include in its proxy materials the Web site address where solicitation materials related to a security holder nominee may be found. Are there other steps that we should take to provide for or encourage the use of electronic means for these elections?

12. How Would the Proposed Rule Apply to Investment Companies?

a. Application of the Security Holder Nomination Procedure to Investment Companies

We are proposing to apply the security holder nomination procedure in proposed Exchange Act Rule 14a-11 to funds. Funds currently are required to comply with the proxy rules under the Exchange Act when soliciting proxies, including proxies relating to the election of directors.¹⁴⁸ As in the case of operating companies, the proposed rules are intended to improve the ability of fund security holders to participate meaningfully in the nomination and election of directors. The nomination procedure would apply to funds in the same manner that it would apply to operating companies, with the following modifications to reflect the different circumstances and reporting requirements applicable to funds.

As in the case of operating companies, the proposed nomination procedure would become operative for a fund only after the occurrence of one or both of the nomination procedure triggering events described above.¹⁴⁹ Funds would be required to provide disclosure regarding the occurrence of these nomination procedure triggering events parallel to that required for operating companies. However, because funds do not file quarterly reports on Exchange Act Form 10-Q, the disclosure would be included on Form N-CSR, which funds file semi-annually.¹⁵⁰ We also are proposing to require disclosure in Form N-CSR regarding each matter submitted to a vote of security holders similar to that currently required by Item 4 of Part II of Exchange Act Form 10-Q, and to delete as duplicative Item 77C of Form N-SAR, which currently requires similar disclosure.¹⁵¹

As with operating companies, if the fund did not hold an annual meeting during the prior year, or if the date of the meeting has changed more than 30 days from the prior year, then the nominating security holder would be required to provide notice a reasonable time before the fund mails its proxy materials for the current year, as specified by the fund in an Exchange Act Form 8-K filed pursuant to proposed Item 13.¹⁵² The fund also would be required to disclose the date of the meeting in Item 13 of Exchange Act Form 8-K. Although funds generally are not required to file on Exchange Act Form 8-K, we are proposing to require them to file on Exchange Act Form 8-K for this limited purpose, in order to help ensure that security holders are made aware in a timely manner of the date by which they must submit a notice of intent to nominate a director.¹⁵³

The proposals would require any nominating security holder or group of security holders to represent that its nominee to the board of a fund is not an "interested person" of the fund as defined in Section 2(a)(19) of the Investment Company Act, rather than independent under the listing standards of a national securities exchange or national securities association, as in the case of operating companies.¹⁵⁴ This "interested person" test also would apply to nominees by a security holder or security holder group for election to the board of directors of a business development company.¹⁵⁵ We are proposing to substitute the Section 2(a)(19) test for the test applied to operating companies because this test is tailored to capture the broad range of affiliations with investment advisers, principal underwriters, and others that are relevant to "independence" in the case of funds.

Because security holders of a mutual fund are not required to file Exchange

which are not required to file Form N-CSR, would provide the required disclosure regarding matters submitted to a vote of security holders, and the new disclosure regarding the occurrence of any of the nomination procedure triggering events, under Item 102B of Form N-SAR. See proposed Instruction to Item 102B of Form N-SAR.

¹⁵² Proposed Item 13 of Exchange Act Form 8-K; Instruction 5 to proposed Exchange Act Rule 14a-11(a).

¹⁵³ See proposed Exchange Act Rule 13a-11(b)(2) and 15d-11(b)(2).

¹⁵⁴ See proposed Exchange Act Rule 14a-11(c)(4); 15 U.S.C. 80a-2(a)(19).

¹⁵⁵ Business development companies are a category of closed-end investment company that are not registered under the Investment Company Act, but are subject to certain provisions of that Act. See Sections 2(a)(48) and 54-65 of the Investment Company Act [15 U.S.C. 80a-2(a)(48) and 80a-53-64].

Act Schedule 13G, the proposals would require a nominating security holder or security holder group for a mutual fund to include the following information, similar to certain information that would otherwise be required on Exchange Act Schedule 13G, as part of the notice to the fund of the security holder's intent to require its nominee on the company's proxy card:¹⁵⁶

- The percentage of each class of securities of the fund that the individual owns beneficially, directly or indirectly, and the number of shares as to which the person has:

- Sole power to vote or to direct the vote;
- Shared power to vote or to direct the vote;
- Sole power to dispose or to direct the disposition of such shares; and
- Shared power to dispose or to direct the disposition of such shares;¹⁵⁷ and

- A certification, signed by each person on whose behalf the notice is filed or his or her authorized representative, that the securities have been held continuously for at least three years.¹⁵⁸

This information would be in addition to the information required to be included in the security holder notice by any nominating security holder or member of a nominating security holder group.¹⁵⁹ The security holder notice, as well as any soliciting material published, sent, or given to security holders in connection with the formation of a nominating security holder group, would be required to be filed under the fund's Investment Company Act file number.¹⁶⁰

We note that the proposed security holder nomination procedure is consistent with the provisions in several of our exemptive rules under the Investment Company Act that require independent directors of funds relying on those rules to select and nominate any other independent directors.¹⁶¹ As discussed above, the proposed security

¹⁵⁶ See proposed Exchange Act Rule 14a-11(c)(11).

¹⁵⁷ For purposes of determining the amount of outstanding securities of a class of equity securities, the security holder generally could rely upon information set forth in the fund's most recent report on Form N-CSR. See proposed Instruction to Exchange Act Rule 14a-11(c)(11)(i).

¹⁵⁸ See proposed Exchange Act Rule 14a-11(c)(11)(ii).

¹⁵⁹ See proposed Exchange Act Rule 14a-11(c)(9).

¹⁶⁰ See proposed Exchange Act Rules 14a-11(f)(1)(iii) and 14a-11(f)(2)(iii).

¹⁶¹ See Release No IC-24816 (Jan. 2, 2001) [66 FR 3734, 3737] (adopting a requirement that independent directors of funds select and nominate any other independent directors as a condition of relying on Investment Company Act Rules 10f-3, 12b-1, 15a-4(b)(2), 17a-7, 17a-8, 17d-1(d)(7), 17e-1, 17g-1(j), 18f-3, or 23c-3).

¹⁴⁸ See Investment Company Act Rule 20a-1 [17 CFR 270.20a-1] (requiring funds to comply with Regulation 14A, Schedule 14A, and all other rules and regulations adopted pursuant to Section 14(a) of the Exchange Act that would be applicable to a proxy solicitation if it were made in respect of a security registered pursuant to Section 12 of the Exchange Act).

¹⁴⁹ See Section II.A.3., above.

¹⁵⁰ Proposed Item 8 of Form N-CSR.

¹⁵¹ Proposed Items 8(a), (b), (c), and (d) of Form N-CSR. Small business investment companies,