

argued that small funds should not be required to bear the burden and costs of providing proxy voting disclosure, when many much larger institutional investors, such as pension plans, insurance companies, common and collective trust funds, and hedge funds would not be required to do so.¹⁰⁵ On the other hand, an association of "socially responsible" funds commented that some smaller fund companies have been providing proxy voting disclosure for some time, with little cost to their investors.¹⁰⁶

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.¹⁰⁷ Approximately 205 out of 3700 investment companies that will be affected by this rule meet this definition.¹⁰⁸

D. Reporting, Recordkeeping, and Other Compliance Requirements

The amendments require a fund to disclose in its SAI (and in Form N-CSR, in the case of a closed-end fund) the policies and procedures it uses to determine how to vote proxies for the securities held in its portfolio, and to provide disclosure in its SAI regarding the availability of its proxy voting record to shareholders. The amendments also require a fund to file with the Commission, on Form N-PX, its complete proxy voting record for its most recent twelve-month period ended June 30. Finally, the amendments require a fund to include in its annual and semi-annual reports to shareholders disclosure that a description of the policies and procedures that the fund uses to determine how to vote proxies relating to portfolio securities 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 SEC Web site. The amendments also require a fund to state in its registration statement and reports to shareholders that its proxy voting record is available (i) without charge, upon

request, by calling a specified toll-free (or collect) telephone number; or on or through the fund's Web site at a specified Internet address; or both; and (ii) on the SEC Web site.

The Commission estimates some one-time formatting and ongoing costs and burdens that will 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 Form N-PX; and disclosing voting records through Web site disclosure or upon request. These costs 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 the collection of proxy voting information on a basis at least as current as annually and, therefore, that the marginal cost increases for most funds will be minimal.

E. Agency Action To Minimize Effect on 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 disclosure amendments will 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 required by the amendments to be provided to shareholders by all funds, not just funds that are not considered small entities.

We have endeavored through the 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 amendments to the

same degree as other investment companies. Further clarification, consolidation, or simplification of the amendments 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.

We note, however, that we have modified our proposals in response to comments, in part to reduce the regulatory burden on funds, including small funds. As adopted, our amendments will require a fund to provide disclosure of its proxy voting record annually on Form N-PX, rather than semi-annually. In addition, we are not adopting the proposed requirement that a fund's annual and semi-annual reports to shareholders include all votes that are inconsistent with the fund's proxy voting policies and procedures. Further, we are modifying our proposed requirement that a fund must send its proxy voting record without charge and upon request, by permitting a fund to make its proxy voting record available on or through its Web site instead.

VIII. Statutory Authority

The Commission is adopting 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]. The Commission is adopting new rule 30b1-4 and new Form N-PX pursuant to authority set forth in Sections 8, 30, 31, and 38 of the Investment Company Act [15 U.S.C. 80a-8, 80a-29, 80a-30, and 80a-37].

List of Subjects

17 CFR Parts 239 and 249

Reporting and recordkeeping requirements, Securities.

17 CFR Parts 270 and 274

Investment companies, Reporting and recordkeeping requirements, Securities.

Text of Rule and Form Amendments

For the reasons set out in the preamble, the Commission amends Title 17, Chapter II of the Code of Federal Regulations as follows:

¹⁰⁵ Letter of Richard Mason, General Counsel, Mosaic Funds (Nov. 27, 2002).

¹⁰⁶ Letter of Timothy H. Smith, President and Chair, Social Investment Forum, at 3 (Nov. 11, 2002).

¹⁰⁷ 17 CFR 270.0-10.

¹⁰⁸ This estimate is based on figures compiled by the Commission's staff regarding investment companies registered on Form N-1A, Form N-2, and Form N-3.