

SECURITIES AND EXCHANGE COMMISSION

17 CFR Parts 270 and 275

[Release Nos. IC-25925, IA-2107; File No. S7-03-03]

RIN 3235-A177

Compliance Programs of Investment Companies and Investment Advisers

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rule.

SUMMARY: The Securities and Exchange Commission is publishing for comment new rules under the Investment Company Act of 1940 and the Investment Advisers Act of 1940 that would require each investment company and investment adviser registered with the Commission to adopt and implement policies and procedures reasonably designed to prevent violation of the federal securities laws, review those policies and procedures annually for their adequacy and the effectiveness of their implementation, and appoint a chief compliance officer to be responsible for administering the policies and procedures. The Commission also seeks comment on other ways to involve the private sector in fostering compliance by investment companies and investment advisers with the federal securities laws. The proposed rules are designed to protect investors by being the first step towards enhanced compliance achieved through private initiative.

DATES: Comments must be received on or before April 18, 2003.

ADDRESSES: To help us process and review your comments more efficiently, comments may be sent to us in either paper or electronic format. Comments should not be sent by both methods.

Comments in paper format should be submitted in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-0609. Comments in electronic format may be submitted at the following e-mail address: rule-comments@sec.gov. All comment letters should refer to File No. S7-03-03; 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 will also be

posted on the Commission's Internet Web site (<http://www.sec.gov>).¹

FOR FURTHER INFORMATION CONTACT:

Hester Peirce, Senior Counsel, Office of Regulatory Policy at (202) 942-0690, or Jamey Basham, Special Counsel, Office of Investment Adviser Regulation at (202) 942-0719.

SUPPLEMENTARY INFORMATION: The Securities and Exchange Commission ("SEC" or "Commission") is requesting public comment on proposed rule 38a-1 [17 CFR 270.38a-1] under the Investment Company Act of 1940 [15 U.S.C. 80a] ("Investment Company Act"), proposed rule 206(4)-7 [17 CFR 275.206(4)-7] under the Investment Advisers Act of 1940 [15 U.S.C. 80b] ("Investment Advisers Act" or "Advisers Act"), and proposed amendments to rule 204-2 under the Advisers Act [17 CFR 275.204-2].

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I. Background

Mutual funds and other types of investment companies provide access to the capital markets for millions of small and large investors.² The tremendous

growth of funds reflects the confidence investors have in funds and the regulatory protections provided by the federal securities laws.

The Commission regulates mutual funds and other investment companies under the Investment Company Act, and regulates the investment advisers that provide investment management services to those funds and to other clients under the Advisers Act.³ The Investment Company Act provides a comprehensive regulatory structure designed to protect largely passive investors in funds, while the Advisers Act, which contains a less detailed regulatory scheme, imposes a broad fiduciary duty on advisers, requiring them to act in the best interest of their clients.⁴ These statutes contain common elements: they require registration with us;⁵ proscribe certain types of harmful conduct;⁶ and give us the authority to require the disclosure of certain information⁷ and the maintenance of certain records.⁸ They give us authority to examine the records of funds and advisers.⁹ During fiscal year 2002, our staff conducted examinations of 278 fund complexes¹⁰ and 1,570 investment advisers.

The Commission's examination of funds and advisers is a key element of our investor protection program. During

³ Funds and advisers are also subject to other federal securities laws, including the Securities Act of 1933 [15 U.S.C. 77] and the Securities Exchange Act of 1934 [15 U.S.C. 78] ("Exchange Act").

⁴ *Transamerica Mortgage Advisors v. Lewis*, 444 U.S. 11, 17 (1979).

⁵ See Section 8(a) of the Investment Company Act [15 U.S.C. 80a-8(a)] and section 203 of the Advisers Act [15 U.S.C. 80b-3].

⁶ See, e.g., sections 10(f) [15 U.S.C. 80a-10(f)] (prohibiting funds from acquiring securities during the existence of an underwriting syndicate in which an affiliate participates), 12(d) [15 U.S.C. 80a-12(d)] (prohibiting funds from acquiring securities of other funds above certain limits), and 17(a) [15 U.S.C. 80a-17(a)] (prohibiting certain persons from engaging in certain purchase, sale, and loan transactions with an affiliated fund) of the Investment Company Act; and section 206 of the Advisers Act [15 U.S.C. 80b-6] (prohibiting fraud).

⁷ See, e.g., section 30(e) of the Investment Company Act [15 U.S.C. 80a-29(e)] (authorizing Commission to require funds to transmit certain information to stockholders) and section 204 of the Advisers Act [15 U.S.C. 80b-4] (authorizing Commission to require advisers to disseminate certain information).

⁸ See Section 31(a) of the Investment Company Act [15 U.S.C. 80a-30(a)] (authorizing Commission to require funds to maintain records) and section 204 of the Advisers Act (authorizing Commission to require advisers to maintain records).

⁹ See Section 31(b) of the Investment Company Act [15 U.S.C. 80a-30(b)] (authorizing Commission to examine fund records) and section 204 of the Advisers Act (authorizing Commission to examine adviser records).

¹⁰ In this release, we use the term "fund complex" to indicate a group of funds that share a compliance program and often also have a common investment adviser or distributor.

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 In this release, we use the term "fund" to mean a registered investment company or a business development company defined in section 2(a)(48) of the Investment Company Act [15 U.S.C. 80a-2(a)(48)], and the term "mutual fund" to mean a registered investment company that is an open-end management company defined in section 5(a) of the Investment Company Act [15 U.S.C. 80a-5(a)].