

**NEW PROSPECTUS DISCLOSURE REQUIREMENTS;
ICI PROVIDES ADDITIONAL GUIDANCE ON USE OF SUMMARY PROSPECTUS**

In January 2009, the Securities and Exchange Commission (the “SEC”) published long-anticipated amendments to Form N-1A and rule 498 under the Securities Act of 1933 (the “Securities Act”).¹ These amendments are intended to provide for the use of a new “summary prospectus” containing key information about open-end funds and to require a summary section in the complete prospectus that is essentially the same as the standalone summary prospectus. At the same time, the SEC also published changes to several items on Form N-1A to acknowledge certain special instructions for exchange-traded funds (“ETFs”) that use that form.

The amendments will be mandatory for all Form N-1A filings made on or after January 1, 2010. Funds can voluntarily comply with them beginning March 31, 2009.

This memorandum provides an overview of the amendments and the new summary prospectus delivery option as well as several updates from a recent Investment Company Institute (the “ICI”) webinar.

Overview

Summary prospectus. The most significant change resulting from the SEC’s amendments is the introduction of a “summary prospectus” delivery option. The SEC revised rule 498 to permit - but not require - funds to deliver a summary prospectus that provides the following key information about the fund in exactly this order:

1. Investment objectives/goals
2. Fee table
3. Investments, risks, and performance
4. Management
5. Purchase and sale of fund shares
6. Tax information
7. Financial intermediary compensation

¹ *Enhanced Disclosure and New Prospectus Delivery Option*, Securities Act Release No. 33-8998, 74 Fed. Reg. 4546 (Jan. 26, 2009) (the “Adopting Release”). The Adopting Release is available at www.sec.gov/rules/final/2009/33-8998.pdf.

The SEC also recently adopted final rules mandating eXtensible Business Reporting Language (“XBRL”) filings for domestic and foreign public companies. XBRL is an open standard electronic format that defines or “tags” data using standard definitions. The final rules were adopted substantially as proposed. Please see our firm’s Client Memorandum, “SEC Issues Final Rules Mandating XBRL Filings,” available at http://www.willkie.com/files/SEC_Issues_Final_Rules_Mandating_XBRL_Filings.pdf.

The SEC did not set a limit on how long the summary prospectus should be, but stated its intention for it to be approximately three or four pages long.²

While using the summary prospectus to satisfy a fund's prospectus delivery obligation is optional, on a recent presentation to ICI members, Paul Schott Stevens, President of the ICI, strongly encouraged funds to do so.³

Liability/Incorporation by reference. One criticism of the SEC's previous attempt at encouraging more streamlined disclosure to mutual fund shareholders – the “profile prospectus” – was that funds were not permitted to incorporate other disclosures into the profile prospectus by reference and, therefore, refrained from using it because of concerns about potential exposure to claims that they omitted information in that document. In adopting the summary prospectus amendments, the SEC explicitly permitted a fund to incorporate disclosure from its statutory prospectus, Statement of Additional Information (“SAI”), and most recent shareholder reports into its summary prospectus by reference.⁴ The SEC apparently believes that the incorporation by reference should address liability concerns.

To incorporate disclosure in one of these documents into the summary prospectus, a fund must make the documents available on-line, together with the fund's summary prospectus, for a specified period of time. The fund also would have to provide standard legends, as well as hyperlinks to specific sections to disclosure in the other documents.⁵ We note that developing or modifying a system to provide the required hyperlinks among the various sections of numerous documents and keeping them current might present a significant technical and operational challenge among all fund complexes, regardless of size.⁶ We also note that judgment will be necessary to properly summarize a fund's risks.

² On the ICI Webinar, Susan Nash, Associate Director of the SEC's Division of Investment Management, confirmed that funds can look to the model summary prospectus published by the SEC when it proposed the summary prospectus rules as an indication of what an acceptable summary prospectus might look like. As discussed below, the final rule changed some of the content of that summary (most notably by removing the disclosure of a fund's top ten holdings). In addition, Ms. Nash stressed that funds have the flexibility to use different formatting techniques than those used by the SEC. ICI Summary Prospectus Webinar (Feb. 12, 2009) (the “ICI Webinar”).

³ ICI Webinar.

⁴ In the Adopting Release, the SEC stated that if a fund incorporates by reference a part of a document, the Summary Prospectus legend must clearly identify the part by page, paragraph, caption, or otherwise. *See* Rule 498(b)(1)(v)(B).

⁵ Revised Rules 498(c)(4), (d)(4), and (e).

⁶ On the ICI Webinar, it was noted that operational and technical efforts to support the required hyperlinking features in the summary prospectus will likely play a key role as to when a fund complex can begin distributing the summary prospectus to investors. ICI Webinar.

The SEC confirmed in the Adopting Release that delivering a summary prospectus in compliance with rule 498 will satisfy a fund's obligations under various statutory provisions to deliver a statutory prospectus.⁷ If a shareholder requests, the fund must also send a paper version of the statutory prospectus within three days of the request. The fund must also post its statutory prospectus, its SAI, and its annual reports to shareholders on the Internet.⁸

Form N-1A amendments. When the N-1A amendments become mandatory in 2010, every mutual fund will have to include a summary section at the beginning of its Form N-1A statutory prospectus.⁹ The content of this summary section is almost identical to that of the summary prospectus (discussed above). For the most part, the amendments to Form N-1A do not change the substantive disclosure that funds already make but instead reorder some items, in particular the fee table.

Like the summary prospectus, the summary section must be presented in a standardized order and must be written in plain English. Fund complexes currently using one integrated statutory prospectus for multiple funds must include a separate summary section for each fund, although the tax and distribution and intermediary compensation disclosure that is identical for all the funds can be combined.¹⁰ This requirement for separate summary sections may be the most controversial of the changes adopted, and is likely to require the most time and effort for compliance. The non-integration requirement applies at the fund or series level, not at the class level, for funds now using integrated multi-fund prospectuses. Funds with multiple share classes, each with its own cost structure, may present summary information separately for each class, integrate the information for multiple classes, or use another presentation consistent with disclosing the information in a standard order at the beginning of the statutory prospectus.

⁷ Specifically, the SEC stated that a fund can satisfy its delivery obligations under Sections 5(b) and 10 of the Securities Act and, for purposes of Section 5(b)(1) of the Securities Act, Section 24(g) of the Investment Company Act of 1940, if it delivers a summary prospectus and otherwise is in compliance with rule 498. The SEC also explained that there is no Section 11 liability for the summary prospectus, although the fund's registration statement, including the mandatory summary section contained in it, would be subject to potential Section 11 liability. See Adopting Release, pages 111-12.

⁸ In addition, the summary prospectus must be given equal or greater prominence than any accompanying materials, but no individual summary prospectus has to be given greater prominence than any other one or any statutory prospectus.

⁹ In the Adopting Release, the SEC stated that post-effective amendments to existing registration statements filed to comply with the amendments to Form N-1A should be filed as 485(a) filings. In appropriate circumstances, however, the SEC will consider requests by existing funds to file these post-effective amendments as 485(b) filings. For example, where a fund complex has previously made 485(a) filings for the post-effective amendments for a number of funds that implement the new requirements, the staff may decide not to review additional such filings by the fund complex.

¹⁰ Specifically, the following sections can be combined in the summary section if the disclosure is identical: information regarding the purchase and sale of fund shares (Item 6 of Revised Form N-1A), tax information (Item 7 of Revised Form N-1A), and financial intermediary compensation (Item 8 of Revised Form N-1A). These items are summarized below. If a fund complex combines these disclosures, it must include the following legend in the summary section for each fund:

For important information about [purchase and sale of fund shares,] [tax information,] and [financial intermediary compensation], please turn to [identify section heading and page number of prospectus].

The following is an outline of the SEC's Form N-1A amendments requiring a summary section of Form N-1A. Amendments that relate only to ETFs are discussed separately below.

1. **Investment objectives/goals.**¹¹ This item is the same as current Item 2(a) of Form N-1A.
2. **Fee table.**¹² In adopting this controversial change, the SEC said it had decided to give the fee table greater prominence by placing it immediately after investment objectives and goals. In the SEC's view, this change will highlight the importance that fees have on investment returns, which it found outweighed the arguments against this requirement that were submitted by many commenters.

In addition to relocating the fee table, the SEC changed some of the information that must be presented in this item:

- *Shareholder fees - new legend regarding sale charge discounts.* If applicable, a mutual fund must include the following legend to highlight the availability of sales charge discounts:

You may qualify for sales charge discounts if you and your family invest, or agree to invest in the future, at least \$[_____] in [name of fund family] funds. More information about these and other discounts is available from your financial professional and in [identify section heading and page number] of the Fund's prospectus and [identify section heading and page number] of the Fund's statement of additional information.
- *Parenthetical following "Annual Fund Operating Expenses."* The SEC revised the text in the parenthetical that must follow the header "Annual Operating Expenses" to read: "expenses that you pay each year as a percentage of your investment."¹³
- *Expense reimbursements and fee waivers.* The basic fee table format has been expanded to explicitly include lines for a fee waiver/reimbursement and net fees. The waiver or reimbursement could be shown in the table as long as it would continue for at least one year from the date of the prospectus. If a fund includes those items, it also must disclose the period for which the fee waiver is expected to continue, including any termination date, and who has the right to terminate and under what condition.
- *Portfolio turnover.* Disclosure about portfolio turnover rates has not changed, but has been moved into the fee table section from current Item 8.¹⁴

¹¹ Item 2 of Revised Form N-1A.

¹² Item 3 of Revised Form N-1A.

¹³ In the current Form N-1A, the parenthetical is required to read: "(expenses that are deducted from Fund assets)."

¹⁴ Item 8 has been redesignated Item 13 in the Revised Form N-1A.

- 3. Investments, risks, and performance.**¹⁵ The only substantive change to this item, other than its placement after the fee table, is to require that a mutual fund that posts updated performance data on the Internet or elsewhere must disclose where to find that information.¹⁶

Funds will need to consider their risk disclosure for purposes of this item. The SEC appears to expect, given its stated intent that the summary prospectus (and the summary section of the Form N-1A statutory prospectus) be three to four pages long, that mutual funds will provide a two or three sentence summary of each risk and will incorporate by reference additional disclosure of each risk factor from the fund's statutory prospectus.

- 4. Management.**¹⁷ As they currently do, funds will identify in the summary section all investment advisers, sub-advisers, and portfolio managers (up to five individual portfolio managers, if they work in a team) to the fund.¹⁸ If there are three or more sub-advisers, only sub-advisers that are responsible for managing a significant portion of the fund's assets (*i.e.*, 30% or more) must be identified.

- 5-6. Purchase and sale of fund shares¹⁹ and Tax information.**²⁰ These disclosure items have not changed from the current version of Form N-1A. However, they will now be included in the summary.

- 7. Financial intermediary compensation.**²¹ The only change to this item is to require a fund that pays distribution or related services fees (including revenue sharing arrangements) to include the following legend:

Payments to Broker-Dealers and Other Financial Intermediaries. If you purchase the Fund through a broker-dealer or other financial intermediary (such as a bank), the Fund and its related companies may pay the intermediary for the sale of Fund shares and related services. These payments may create a conflict of interest by influencing the broker-dealer or other intermediary and your salesperson to recommend the Fund over another investment. Ask your salesperson or visit your financial intermediary's Web site for more information.

¹⁵ Item 4 of Revised Form N-1A.

¹⁶ Item 4(b)(2)(i) of Revised Form N-1A. In addition, in a change from its proposal, the SEC will not require disclosure of a fund's top ten holdings in the summary section or require the summary prospectus to be updated quarterly. The SEC staff said that in focus group testing, some investors indicated that this information may have limited value in a summary document because a fund's top ten portfolio holdings information changes frequently and can quickly become outdated, even if updated quarterly.

¹⁷ Item 5 of Revised Form N-1A.

¹⁸ More detailed disclosure about their background and experience, and the services they provide, is required in Item 10 of the Revised Form N-1A, and would be part of the fund's statutory prospectus but not its summary prospectus.

¹⁹ Item 6 of Revised Form N-1A.

²⁰ Item 7 of Revised Form N-1A.

²¹ Item 8 of Revised Form N-1A.

Ticker Symbol. In addition, while not directly related to the adoption of the summary prospectus, the SEC amended Item 1 of Form N-1A to require funds to disclose their ticker symbols on the cover page of the statutory prospectus and on the front of the SAI. The ticker symbol must also appear on the cover page or beginning of the summary prospectus.²² If the document relates to multiple funds or multiple classes, ticker symbols for each must be disclosed. EDGAR users may find this useful because EDGAR filings are indexed by ticker symbol and ticker symbols may be used as search terms in EDGAR searches.

Amendments for ETF disclosure. The SEC also adopted amendments to the several items in Form N-1A to make them more relevant to ETFs, in particular to take into account the fact that most investors purchase ETFs in secondary market transactions and do not transact in “creation units” of ETF shares.²³ For example, the amendments eliminate the need to disclose in the statutory prospectus how the ETF’s purchase and redemption procedures work because most investors purchase ETF shares on secondary markets. Information about those procedures would be disclosed in the fund’s SAI.

In addition, ETFs must disclose the number of shares contained in a creation unit (*i.e.*, the aggregate number of shares used in an ETF’s direct purchase and redemption transactions), that individual ETF shares can only be traded on the secondary market through a broker-dealer, that ETF shares can trade at a premium or discount to the ETF’s NAV, and that shareholders may receive more or less than net asset value (“NAV”) when buying and selling ETF shares.²⁴

Fee table disclosure in Form N-1A also was amended to exclude fees and expenses for purchases or redemptions of creation units. The narrative explanation preceding the example in the fee table must state that investors in ETF shares may pay brokerage commissions that are not reflected in the example.

Finally, ETFs must provide a table showing the frequency with which market prices of fund shares have tracked the fund’s NAV.²⁵ Specifically, the ETF must disclose the number of trading days during the most recently completed calendar year (and any quarters since that year) on which the “market price” (as defined)²⁶ of the ETF shares was higher than the fund’s NAV and the number of days on which it was lower than the fund’s NAV. This information concerning the premium or discount must be expressed as a percentage of the NAV of the ETF. The table can be published on the ETF’s website instead of in the ETF’s prospectus, in which

²² Amended Rule 498(b)(1). The fund’s name and the class or classes to which the summary prospectus relates must also appear on the cover page or at the beginning of the summary prospectus.

²³ In addition, the SEC adopted definitions of the terms “Exchange-Traded Funds” and “Market Price” for purposes of Form N-1A.

²⁴ The SEC adopted this requirement in lieu of its proposal to require ETFs to disclose market price returns of the ETF shares in addition to returns based on the ETF’s NAV. The SEC agreed with commenters that this information may not be relevant to many ETF investors.

²⁵ Item 11(g)(2) of Revised Form N-1A.

²⁶ The “market price” would be either the closing price on the principal market on which the ETF shares trade or the range between the highest offer and the lowest bid if that price more accurately reflects the current market value of the fund’s shares at the time the Fund calculates its NAV.

case the prospectus must contain the address of the website where the information can be located.

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