

April 22, 2004

Memorandum To Clients and Friends

**New Shareholder Expense and Portfolio Disclosure
Requirements in Shareholder Reports**

Introduction

The Securities and Exchange Commission (the “SEC”) recently adopted new requirements relating to disclosure of expenses and portfolio investments in reports to shareholders of a registered investment company (“fund”).¹ The amendments:

- require open-end funds to disclose in shareholder reports fund expenses borne by shareholders during the reporting period covered in the report;
- permit funds to include in shareholder reports a summary portfolio schedule in lieu of a schedule of all a fund’s portfolio holdings;
- require qualitative information in shareholder reports about a fund’s portfolio holdings in a tabular or graphic presentation by identifiable categories; and
- require funds to file a complete portfolio schedule for the second and fourth quarters of a fiscal year on Form N-CSR and for the first and third fiscal quarters, when the semi-annual report on Form N-CSR is not filed, a complete portfolio schedule on new Form N-Q.²

¹ For open-end funds, the new disclosure requirements are in Item 21 of Form N-1A. Item 21 has historically been the repository for shareholder report disclosure requirements relating generally to financial statement information rather than Rule 30e-1 under the Investment Company Act of 1940 (“1940 Act”), which implements the shareholder reporting requirements under Section 30(e) of the 1940 Act. Similarly, for closed-end funds, the new requirements are in Item 23 of Form N-2.

² The SEC amendments also eliminate the option to include the Management’s Discussion of Fund Performance in either a fund’s prospectus or in an annual shareholder report and require that it be included in the annual report.

Compliance Dates

- Effective Date of the new disclosure requirements and reporting requirements: **May 10, 2004.**
- Compliance Date for first shareholder report and filing of Form N-CSR or for filing Form N-Q for first or third quarter: **Periods ending on or after July 9, 2004.**

New Disclosure in Shareholder Reports

1. Fund Expense Information

The amendments require open-end funds to disclose in shareholder reports fund expenses during the reporting period covered in the report. Specifically, a fund must disclose in tabular format:

- the cost of expenses in dollars based on the fund's actual expenses and return for the period reflecting a beginning account value of \$1,000; and
- for the purposes of comparison to other funds, the cost of expenses in dollars based on the fund's actual expenses for the period and a hypothetical return of 5% per year.

The following is an example of the expense table based on a fund return of 18.4% and an annualized expense ratio of 1.09%:

Example

	Beginning Account Value 9/30/03	Ending Account Value 3/31/04	Expenses Paid During Period*
Fund Actual	\$1,000	\$1,178	\$6
Hypothetical 5% Return	\$1,000	\$1,019	\$6

*Expenses are equal to the fund's annualized expense ratio of 1.09%, multiplied by the average account value over the period, multiplied by 183/366 (to reflect the one-half year period between September 30, 2003 and March 31, 2004).

The expense table must be preceded by a prescribed narrative explanation of the types of costs charged by the fund, how a shareholder can calculate actual expenses based on the shareholder's account value, the hypothetical example, and the distinction between operational costs, which are reflected in the table, and transactional costs, which are not reflected in the table. The narrative explanation is required to be

modified to accurately reflect a fund's circumstances and may be modified if it contains comparable information to the prescribed explanation.

The methodology for calculating the example is similar, but not identical, to the methodology for calculating the expense example in the fee table included in a fund's prospectus. One important difference is that, unlike the fee table, actual expenses can reflect expenses after fee waiver or expense reimbursement. The limitation that only contractual waivers can be reflected, as in the prospectus fee table, will not be applicable. No additional disclosure regarding expenses before waiver or reimbursement is required. If a fund includes more than one class in the shareholder report, a separate example will be required for each class.

2. *Disclosure of Portfolio Holdings*

a. Summary Portfolio Schedule

Responding to long-standing requests from the fund industry, the SEC will permit funds to include a summary portfolio schedule in shareholder reports in lieu of the full schedule of portfolio investments.³ The industry sought this change because supplying the complete list was costly and could, for example, be more than 20 pages in a shareholder report for a fund with a large number of portfolio investments. These costs were particularly acute for index funds. In addition, the full list did not provide information in a way that would enable shareholders to identify significant characteristics of a fund's investments. The summary portfolio schedule combined with the qualitative portfolio disclosure discussed below should provide better information to shareholders at less cost.

The summary portfolio schedule must include a fund's 50 largest holdings and investments in issuers that are greater than one percent of the fund's net asset value. Securities in the summary portfolio schedule must be identified by categories rather than listed in order of the size of holding. The categories include (i) the type of investment, such as common stocks, preferred stocks, debt securities, and (ii) the related industry, country or geographic region of the investment.⁴

A fund that uses a summary portfolio schedule is required to file its complete portfolio schedule with the SEC on Form N-CSR. A fund also is required to disclose in shareholder reports that complete portfolio schedules are available upon request,

³ The SEC also exempted money market funds from all portfolio schedule disclosure requirements because they are not necessary in view of the limitations on their investments under Rule 2a-7. Money market funds will be required to make the schedule available to shareholders upon request and free of charge, and disclose the availability of the schedule in their reports to shareholders.

⁴ The summary portfolio schedule requirements are set forth in Schedule VI under Rule 210.12 of Regulation S-X. There are a number of technical requirements regarding the presentation of portfolio holdings in the schedule, such as aggregation of certain issuances of securities for the purposes of determining the fifty largest issues and aggregation of short-term debt instruments or fully collateralized repurchase agreements.

without charge, (i) by calling a specified toll-free or collect number, (ii) on the fund's website (if applicable) and (iii) on the SEC's website.⁵

b. Qualitative Portfolio Holdings Disclosure

The amendments require funds to include in shareholder reports qualitative disclosure about a fund's portfolio through the use of tables, charts or graphs that depict portfolio holdings by reasonably identifiable categories, such as type of security, industry sector, geographic region, credit quality or maturity.⁶ A fund has flexibility to choose the categories and the format used in the presentation. However, the presentation must be made in a manner reasonably designed to show clearly the types of the fund's investments. A fund must explain the basis of its presentation and include any additional explanatory information necessary to make the presentation understandable. A fund's tabular or graphic presentation must reflect all of the fund's investment activities.

3. *Filing and Certification Requirements*

In a trade-off for the summary portfolio disclosure in shareholder reports, the SEC is requiring the quarterly filing of portfolio holdings to provide investors with access to more frequent information about a fund's investments. The complete portfolio schedule is required to be filed on two different forms depending on the quarter. Funds are required to file a complete portfolio schedule for the second and fourth fiscal quarters on Form N-CSR. Since Form N-CSR is designed for the filing of semi-annual shareholder report information, the SEC adopted a new Form N-Q to serve as the vehicle for the filing of a complete portfolio schedule for the first and third fiscal quarters. Form N-Q must be filed within 60 days of the end of the fiscal quarter.⁷ These schedules may be unaudited.

As with Form N-CSR, Form N-Q was adopted under the Securities Exchange Act of 1934, as well as the 1940 Act, to allow for the certifications required by Section 302 of the Sarbanes-Oxley Act of 2002. The SEC modified the Section 302 certification to require the certifying officer to state, based on the officer's knowledge, that the schedules of investments included in the report fairly present in all material respects the

⁵ A fund must send the complete portfolio schedule to a shareholder within three days of the request and it must be sent by first class mail or other means designed to ensure equally prompt delivery.

⁶ In what appears to be an unnecessary limitation in an otherwise flexible approach, the SEC requires the use of the ratings of only one NRSRO.

⁷ A fund is not required to deliver the Form N-Q to shareholders; however, the fund must disclose in shareholder reports that (i) the fund files its complete schedule of portfolio holdings with the SEC for the first and third quarters of each fiscal year on Form N-Q, (ii) the fund's Form N-Q is available on the SEC's website at <http://www.sec.gov> or may be reviewed and copied at the SEC's Public Reference Room and how information on the operation of the Public Reference Room may be obtained, and (iii) if the fund makes the information on Form N-Q available on its website or by request, information on how a shareholder may obtain the information.

investments of the registrant as of the end of the fiscal quarter for which the report is filed. Form N-Q requires a certifying officer's conclusions about the effectiveness of a fund's disclosure controls and procedures based on an evaluation within 90 days of the filing. A certifying officer must also state that the fund's report discloses any changes in the fund's internal control over financial reporting that occurred during the most recent fiscal quarter.⁸

* * *

If you have any questions, please contact us at (202) 737-8833 for more information.

Kathleen K. Clarke
Nora L. Sheehan

99037.0020 #480015

⁸ Form N-CSR previously required a certifying officer to disclose any change in a fund's internal control over financial reporting that occurred during the fund's most recent fiscal half-year. The amendments change this requirement in Form N-CSR to the fiscal quarter.