

**PAPERWORK REDUCTION ACT**  
**SUPPORTING STATEMENT**

**FORM N-1A**

**A. JUSTIFICATION**

**1. Necessity for the Information Collection**

Millions of individual Americans invest in shares of open-end management investment companies (“mutual funds”),<sup>1</sup> relying on mutual funds for their retirements, their children’s educations, and their other basic financial needs.<sup>2</sup> These investors face a difficult task in choosing among the more than 8,000 available mutual funds.<sup>3</sup> Fund prospectuses, which have been criticized by investor advocates, representatives of the fund industry, and others as long and complicated, often prove difficult for investors to

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<sup>1</sup> An open-end management investment company is an investment company, other than a unit investment trust or face-amount certificate company, that offers for sale or has outstanding any redeemable security of which it is the issuer. *See* Sections 4 and 5(a)(1) of the Investment Company Act [15 U.S.C. 80a-4 and 80a-5(a)(1)].

<sup>2</sup> Investment Company Institute, 2007 Investment Company Fact Book, at 57 (2007), available at: [http://www.icifactbook.org/pdf/2007\\_factbook.pdf](http://www.icifactbook.org/pdf/2007_factbook.pdf) (96 million individuals own mutual funds).

<sup>3</sup> *Id.* at 10 (as of year-end 2006, there were 8,726 mutual funds).

use efficiently in comparing their many choices.<sup>4</sup> Current Commission rules require mutual fund prospectuses to contain key information about investment objectives, risks, and expenses that, while important to investors, can be difficult for investors to extract. Prospectuses are often long, both because they contain a wealth of detailed information and because prospectuses for multiple funds are often combined in a single document. Too frequently, the language of prospectuses is complex and legalistic, and the presentation formats make little use of graphic design techniques that would contribute to readability.

In recent years, numerous commentators have suggested that investment information that is key to an investment decision should be provided in a streamlined

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<sup>4</sup> See William D. Lutz, Ph.D., Professor of English, Rutgers University, Transcript of U.S. Securities and Exchange Commission Interactive Data Roundtable, at 69 (June 12, 2006), available at: <http://www.sec.gov/spotlight/xbrl/xbrlofficialtranscript0606.pdf> (“June 12 Roundtable Transcript”) (stating that current mutual fund prospectus is “unreadable”); Don Phillips, Managing Director, Morningstar, Inc., *id.* at 26 (stating that current prospectus is “bombarding investors with way more information than they can handle and that they can intelligently assimilate”). A Webcast archive of the June 12 Interactive Data Roundtable is available at: <http://www.connectlive.com/events/secxbrl/>. See also Investment Company Institute, Understanding Preferences for Mutual Fund Information, at 8 (Aug. 2006), available at: [http://ici.org/pdf/rpt\\_06\\_inv\\_prefs\\_summary.pdf](http://ici.org/pdf/rpt_06_inv_prefs_summary.pdf) (“ICI Investor Preferences Study”) (noting that sixty percent of recent fund investors describe mutual fund prospectuses as very or somewhat difficult to understand, and two-thirds say prospectuses contain too much information); Associated Press Online, Experts: Investors Face Excess Information (May 25, 2005) (“There is broad agreement . . . that prospectuses have too much information . . . to be useful.” (quoting Mercer Bullard, President, Fund Democracy, Inc.)); Thomas P. Lemke and Gerald T. Lins, The “Gift” of Disclosure: A Suggested Approach for Managed Investments, *The Investment Lawyer*, at 19 (Jan. 2001) (stating that the fund prospectus “typically contains more information than the average investor needs”).

document with other more detailed information provided elsewhere.<sup>5</sup> Furthermore, recent investor surveys indicate that investors prefer to receive information in concise, user-friendly formats.<sup>6</sup>

Similar opinions were voiced at a roundtable held by the Commission in June 2006, at which representatives from investor groups, the mutual fund industry, analysts,

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<sup>5</sup> See Charles A. Jaffe, *Improving Disclosure of Funds Can Be Done*, *The Fort Worth Star-Telegram* (May 7, 2006) (“Bring back the profile prospectus, and make its use mandatory. . . . A two page-summary of [the] key points [in the profile] – at the front of the prospectus – would give investors the bare minimum of what they should know out of the paperwork.”); *Experts: Investors Face Excess Information*, *supra* note Error: Reference source not found (stating “a possible middle ground in the disclosure debate is to rely more heavily on so-called profile documents which provide a two-page synopsis of a fund” (attributing statement to Mercer Bullard, President, Fund Democracy, Inc.)); *Mutual Funds: A Review of the Regulatory Landscape*, Hearing Before the Subcomm. on Capital Markets, Insurance and Government Sponsored Enterprises of the Comm. on Financial Services, U.S. House of Representatives, 109<sup>th</sup> Cong. (May 10, 2005), at 24 (“To my mind, a new and enhanced mutual fund prospectus should have two core components. It should be short, addressing only the most important factors about which typical fund investors care in making investment decisions, and it should be supplemented by additional information available electronically, specifically through the Internet, unless an investor chooses to receive additional information through other means.” (Testimony of Barry P. Barbash, then Partner, Shearman & Sterling LLP)); Thomas P. Lemke and Gerald T. Lins, *The “Gift” of Disclosure: A Suggested Approach for Managed Investments*, *supra* note Error: Reference source not found, at 19 (information that is important to investors includes goals and investment policies, risks, costs, performance, and the identity and background of the manager).

In addition, a mutual fund task force organized by the National Association of Securities Dealers, Inc. (“NASD”) supported the use of a “profile plus” document, on the Internet, that would include, among other things, basic information about a fund’s investment strategies, risks, and total costs, with hyperlinks to additional information in the prospectus. See *NASD Mutual Fund Task Force, Report of the Mutual Fund Task Force: Mutual Fund Distribution* (Mar. 2005), available at: [http://www.finra.org/web/groups/rules\\_regs/documents/rules\\_regs/p013690.pdf](http://www.finra.org/web/groups/rules_regs/documents/rules_regs/p013690.pdf).

<sup>6</sup> See *ICI Investor Preferences Study*, *supra* note Error: Reference source not found, at 29 (“Nearly nine in 10 recent fund investors say they prefer a summary of the information they want to know before buying fund shares, either alone or along with a detailed document . . . . Just 13 percent prefer to receive only a detailed document.”); Barbara Roper and Stephen Brobeck, *Consumer Federation of America, Mutual Fund Purchase Practices*, at 13-14 (June 2006), available at: [http://www.consumerfed.org/pdfs/mutual\\_fund\\_survey\\_report.pdf](http://www.consumerfed.org/pdfs/mutual_fund_survey_report.pdf) (survey respondents more likely to consult a fund summary document rather than a prospectus or other written materials).

and others discussed how the Commission could change the mutual fund disclosure framework so that investors would be provided with better information. Significant discussion at the roundtable concerned the importance of providing mutual fund investors with access to key fund data in a shorter, more easily understandable format.<sup>7</sup> The participants focused on the importance of providing mutual fund investors with shorter disclosure documents, containing key information, with more detailed disclosure documents available to investors and others who choose to review additional information.<sup>8</sup> There was consensus among the roundtable participants that the key information that investors need to make an investment decision includes information

about a mutual fund's investment objectives and strategies, risks, cost, and performance.<sup>9</sup>

<sup>7</sup> See, e.g., Henry H. Hopkins, Vice President and Chief Legal Counsel, T. Rowe Price Group, Inc., June 12 Roundtable Transcript, *supra* note Error: Reference source not found, at 31 (“[S]hareholders prefer receiving a concise summary of fund information before buying.”); William D. Lutz, Ph.D., Professor of English, Rutgers University, *id.* at 88 (stating that “investors [should] be able to find quickly and easily the information they want”).

<sup>8</sup> See Don Phillips, Managing Director, Morningstar, Inc., *id.* at 27 (stating that mutual fund investors need two different documents, including a simplified print document and a tagged electronic document); Paul Schott Stevens, President and Chief Executive Officer, Investment Company Institute, *id.* at 72-73 (urging the Commission to consider permitting mutual funds to “deliver a clear concise disclosure document . . . much like the profile prospectus” with a statement that additional disclosure is available on the funds’ website or upon request in paper); Elisse B. Walter, Senior Executive Vice President, NASD, *id.* at 41 (noting that the industry-recommended disclosure document, the “profile plus,” would include hyperlinks to the statutory prospectus, which would enable investors to “choose for themselves the level of detail they want”).

<sup>9</sup> See Barbara Roper, Director of Investor Protection, Consumer Federation of America, June 12 Roundtable Transcript, *supra* note Error: Reference source not found, at 20 (noting that there is “agreement to the point of near unanimity about the basic

We are proposing an improved mutual fund disclosure framework that is intended to provide investors with information that is easier to use and more readily accessible, while retaining the comprehensive quality of the information that is available today. The foundation of the proposal is the provision to all investors of streamlined and user-friendly information that is key to an investment decision.

To implement this improved disclosure framework, we are proposing amendments to Form N-1A that would require every prospectus to include a summary section at the front of the prospectus, consisting of key information about the fund, including investment objectives and strategies, risks, costs, and performance. This key information has been identified by the participants in the roundtable, by investor research, and by a variety of commentators as information that is important to most investors in selecting mutual funds.<sup>10</sup> The key information would be required to be presented in plain English in a standardized order. Our intent is that this information would be presented succinctly, in three or four pages at the front of the prospectus.

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factors that investors should consider when selecting a mutual fund. These closely track the content of the original fund profile with highest priority given to investment objectives and strategies, risks, costs, and past performance particularly as it relates to the volatility of past returns.”). See also Paul G. Haaga, Jr., Executive Vice President, Capital Research and Management Company, *id.* at 90 (stating that the Commission should “specify some minimum amounts of information” to provide investors with “something along the lines of the [fund] profile”); Henry H. Hopkins, Vice President and Chief Legal Counsel, T. Rowe Price Group, Inc., *id.* at 31 (“The profile is an excellent well organized disclosure document whose content requirements were substantiated by SEC-sponsored focus groups and an industry pilot program.”); William D. Lutz, Ph.D., Professor of English, Rutgers University, *id.* at 88 (noting that the information that mutual fund investors want has not changed substantially since the adoption of the profile); Elisse B. Walter, Senior Executive Vice President, NASD, *id.* at 40-41 (noting that NASD’s “profile plus” builds on the profile and includes key information about a fund’s objectives, risks, fees, and performance, as well as information about dealer fees and conflicts of interest).

<sup>10</sup> See *supra* notes Error: Reference source not found and Error: Reference source not found.

## **2. Purpose of the Information Collection**

The purpose of Form N-1A is to meet the filing and disclosure requirements of the Securities Act of 1933 (“Securities Act”) and the Investment Company Act of 1940 (“Investment Company Act”) and to enable funds to provide investors with information necessary to evaluate an investment in the fund. Unlike many other federal information collections, which are primarily for the use and benefit of the collecting agency, this information collection is primarily for the use and benefit of investors. The information filed with the Commission also permits the verification of compliance with securities law requirements and assures the public availability and dissemination of the information.

## **3. Role of Improved Information Technology**

The Commission’s electronic filing system (Electronic Data Gathering, Analysis and Retrieval or “EDGAR”) is designed to automate the filing, processing and dissemination of full disclosure filings. The system permits publicly held companies to transmit filings to the Commission electronically. This automation has increased the speed, accuracy and availability of information, generating benefits to investors and financial markets. Form N-1A is required to be filed with the Commission electronically on EDGAR. The public may access filings on EDGAR through the Commission’s Internet website (<http://www.sec.gov>) or at EDGAR terminals located at the Commission’s public reference rooms. Prospectuses and statements of additional information (“SAIs”) may be sent to investors by electronic means so long as the fund meets certain requirements.<sup>11</sup> The Commission has no information concerning the

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<sup>11</sup> See Securities Act Release No. 7233 (Oct. 6, 1995) [[60 FR 53458 \(Oct. 13, 1995\)](#)]; Securities Act Release No. 7856 (Apr. 28, 2000) [[65 FR 25843 \(May 4, 2000\)](#)].

percentage of such documents sent electronically, but believes it is a small percentage. Additionally, our proposed rules also include a separate collection of information for proposed rule 498 that would significantly increase the posting of prospectuses on Internet Web sites.

#### **4. Efforts to Identify Duplication**

The Commission periodically evaluates rule-based reporting and recordkeeping requirements for duplication, and reevaluates them whenever it proposes a rule or a change in a rule. The requirements of Form N-1A are not generally duplicated elsewhere.

#### **5. Effect on Small Entities**

The current disclosure requirements for the registration statements and reports on Form N-1A do not distinguish between small entities and other funds. The burden on smaller funds, however, to prepare and file registration statements may be greater than for larger funds. This burden includes the cost of producing, printing, filing, and disseminating the prospectuses and SAIs. The Commission believes, however, that imposing different requirements on smaller investment companies would not be consistent with investor protection and the purposes of the registration statements.

With respect to the proposed amendments, the Commission considered special requirements for small entities. Different disclosure requirements for small entities may create the risk that investors in these funds would be less able to evaluate funds and less able to compare different funds, thereby lessening the ability of investors to make informed choices among funds. We believe it is important for the disclosure that would

be required by the proposed amendments to Form N-1A to be provided to investors in all funds, not just funds that are not considered small entities.

We review all rules periodically, as required by the Regulatory Flexibility Act, to identify methods to minimize recordkeeping or reporting requirements affecting small businesses.

**6. Consequences of Less Frequent Collection**

With the proposed amendments, the frequency with which information from Form N-1A is collected will not change.

**7. Inconsistencies with Guidelines in 5 CFR 1320.5(d)(2)**

Not Applicable.

**8. Consultation Outside the Agency**

Form N-1A has previously been amended through rulemaking actions pursuant to the Administrative Procedures Act. Comments are generally received from registrants, trade associations, the legal and accounting professions, and other interested parties. In addition, the Commission and staff of the Division of Investment Management participate in an ongoing dialogue with representatives of the investment company industry through public conferences, meetings, and informal exchanges. The Commission has solicited and will consider comment on the proposed amendments to enhance the disclosures that are provided to mutual fund investors, and on the collection of information that would be imposed by the amendments.

**9. Payment of Gift to Respondents**

Not Applicable.



**10. Assurance of Confidentiality**

Not Applicable.

**11. Sensitive Questions**

Not Applicable.

**12. Estimate of Hour Burden**

Open-end funds register as investment companies under the Investment Company Act and register their securities under the Securities Act on Form N-1A. Compliance with the disclosure requirements of Form N-1A is mandatory.

The estimate of the annual number of registration statements filed on Form N-1A is based on the average annual number of filings received by the Commission over the past three years. The hour burden estimates for preparing and filing Form N-1A are based on the Commission's experience with the contents of the form. The number of burden hours may vary depending on, among other things, the complexity of the filing and whether preparation of the form is performed by fund staff or outside counsel. The estimated average burden hours are made solely for purposes of the Paperwork Reduction Act and are not derived from a quantitative, comprehensive, or even representative survey or study of the burdens associated with Commission rules and forms.

Form N-1A generally imposes two types of reporting burdens on investment companies: (1) the burden of preparing and filing the initial registration statement; and (2) the burden of preparing and filing post-effective amendments to a previously effective registration statement.

The Commission estimates that the burden hours that will be imposed by Form N-1A are as follows:

### **Calculation of Hour Burden of Initial Form N-1A Filings**

• Number of initial Form N-1A filings annually	104
• Average number of portfolios per filing	3.64
• Number of portfolios/funds referenced in initial Form N-1A filings annually	379
• Current hour burden per portfolio/fund for preparing initial Form N-1A filing	838.47
• Total annual hour burden for initial Form N-1A filings (379 x (838.47))	317,780

### **Calculation of Hour Burden of Post-Effective Amendments**

• Number of post-effective amendments filed annually	2,293
• Average number of portfolios per filing	3.64
• Number of portfolios/funds referenced in post-effective amendments filed annually	8,347
• Current hour burden per portfolio/fund for preparing post-effective amendments	119
• Total annual hour burden to prepare post-effective amendments (8,347 x (119))	993,293

### **Total Annual Hour Burden**

• Annual hours for initial Form N-1A filings + annual hours for post-effective amendments (317,780 + 993,293)	1,311,073
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Based on the estimated wage rate, the total cost to the fund industry of the hour burden for complying with Form N-1A is approximately \$331,045,933.<sup>12</sup>

### **13. Estimate of Total Annual Cost Burden**

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<sup>12</sup> This cost is estimated by multiplying the total annual hour burden (1,311,073 hours) by the estimated hourly wage rate of \$252.50. The estimated wage figure is based on published rates for compliance attorneys and senior programmers, modified to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits, and overhead, yielding effective hourly rates of \$261 and \$244, respectively. See Securities Industry Association, Report on Management & Professional Earnings in the Securities Industry 2006 (Sept. 2006). The estimated wage rate is further based on the estimate that attorneys and programmers would divide time equally, resulting in a weighted wage rate of \$252.50 (((\$261 x .50) + (\$244 x .50))).

Cost burden is the cost of goods and services purchased to prepare and update reports filed on Form N-1A, such as for the services of outside counsel. The cost burden does not include the hour burden discussed in Item 12. Estimates are based on the Commission's experience with the filing of Form N-1A.

The current estimated cost burden for preparing an initial Form N-1A is \$20,300 per portfolio and for preparing a post-effective amendment to a previously effective registration statement is \$8,894 per portfolio. The Commission estimates that, on an annual basis, 379 portfolios will be referenced in initial filings on Form N-1A and 8,347 portfolios will be referenced in post-effective amendments of Form N-1A filings. Thus, the total cost burden allocated to Form N-1A would be as follows:

Cost Burden of Preparing and Filing Initial Form N-1A

- Cost burden per portfolio/fund of preparing and filing initial Form N-1A \$20,300
- Number of portfolios/funds referenced in initial Form N-1A filings annually 379
- Cost burden of preparing and filing portfolio/fund on initial Form N-1A (number of portfolios x cost per portfolio) \$7,693,700

Cost Burden of Preparing and Filing Post-Effective Amendments

- Cost burden per portfolio/fund of preparing and filing post-effective amendments \$8,894
- Number of portfolios/funds referenced in post-effective amendments filed annually 8,347
- Cost burden of preparing and filing portfolio/fund post-effective amendments (number of portfolios x cost per portfolio) \$74,238,218

Total Cost Burden

- Initial Form N-1A + post-effective amendments (\$7,693,700 + \$74,238,218) \$81,931,918

#### **14. Estimate of Cost to the Federal Government**

The annual cost of reviewing and processing new registration statements, and post-effective amendments of investment companies amounted to approximately \$16.8 million in fiscal year 2006, based on the Commission's computation of the value of staff time devoted to this activity and related overhead.

#### **15. Explanation of Changes in Burden**

We estimate that complying with the proposed new disclosure requirements would not entail a significant burden. For the most part, the information that would be required is already required in a fund's prospectus. Therefore, we expect that the cost of compiling and reporting this information should be limited.

The hour burden for Form N-1A is on a per portfolio basis and not per registration statement filed with the Commission.<sup>13</sup> We received 2,397 initial registration statements and post-effective amendments on Form N-1A during our 2006 fiscal year covering approximately 8,726 portfolios. The estimated average hour burden per portfolio for providing the proposed disclosure in a registration statement would be 8 hours per portfolio.

Currently, the total annual hour burden for the industry for preparing and filing registration statements on Form N-1A is 1,575,184 hours. As a result of the proposed amendments to the registration statement forms and the decrease in our estimates of the average annual number of portfolios, the hour burden for preparing and filing initial registration statements and post-effective amendments on Form N-1A will decrease to a total annual burden of 1,311,073 hours.

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<sup>13</sup> These estimates are based upon Commission staff assessment of the proposed amendments in light of the current hour burden and current reporting requirements.

**16. Information Collection Planned for Statistical Purposes**

Not Applicable.

**17. Approval to not Display Expiration Date**

Not Applicable.

**18. Exceptions to Certification Statement**

Not Applicable.

**B. COLLECTIONS OF INFORMATION EMPLOYING STATISTICAL METHODS**

Not Applicable.