

MEMO# 23197

January 21, 2009

SEC Adopts "Summary Prospectus" Rule and Related Amendments to Form N-1A

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TO: ACCOUNTING/TREASURERS COMMITTEE No. 2-09
BANK, TRUST AND RECORDKEEPER ADVISORY COMMITTEE No. 2-09
BOARD OF GOVERNORS No. 2-09
BROKER/DEALER ADVISORY COMMITTEE No. 5-09
ETF ADVISORY COMMITTEE No. 1-09
EXCHANGE-TRADED FUNDS (ETF) COMMITTEE No. 1-09
INVESTMENT COMPANY DIRECTORS No. 2-09
OPERATIONS MEMBERS No. 3-09
PENSION MEMBERS No. 4-09
SEC RULES MEMBERS No. 7-09
SMALL FUNDS MEMBERS No. 6-09
TECHNOLOGY COMMITTEE No. 2-09
TRANSFER AGENT ADVISORY COMMITTEE No. 7-09
VARIABLE INSURANCE PRODUCTS ADVISORY COMMITTEE No. 2-09 RE: SEC ADOPTS
"SUMMARY PROSPECTUS" RULE AND RELATED AMENDMENTS TO FORM N-1A

The Securities and Exchange Commission has adopted amendments to the rules and forms used by open-end management investment companies to register under the Investment Company Act of 1940 and to offer their securities under the Securities Act of 1933. [\[1\]](#) The amendments, which reflect many of the Institute's comments, require key information to appear in plain English, in a standardized order, at the front of every mutual fund's statutory prospectus, in place of the current risk/return summary. Additionally, the amendments permit a fund to satisfy its prospectus delivery obligation under Section 5(b)(2) of the Securities Act by providing investors with a "Summary Prospectus" containing the same key information, and making additional information, including the statutory prospectus, available on the Internet and in paper upon request.

In connection with these amendments, the Commission has also adopted certain provisions originally proposed in connection with its “Exchange-Traded Funds” rule proposal. [2] These provisions amend the Form N-1A disclosure requirements for exchange-traded funds (“ETFs”) registered as open-end management investment companies. Subject to these amendments, these ETFs may use the Summary Prospectus.

The amendments are effective as of March 31, 2009, with compliance required for all initial registration statements and post-effective amendments that add a new series or are annual updates filed on or after January 1, 2010.

The amendments are summarized below. On February 12, 2009, the Institute will host a webinar to discuss the amendments, including legal considerations regarding the use of a Summary Prospectus as an offering document, implementation issues and challenges with respect to technology and working with intermediaries, and operational considerations. More information is available at <http://www.ici.org/pdf/web0109slides.pdf>.

Background

As explained in the Adopting Release, investor advocates, fund industry representatives and others agree that mutual fund prospectuses are long and complicated, and difficult for investors to use. There is widespread agreement that certain key information should be provided to investors in a streamlined document, with more details provided elsewhere. The adopted amendments are intended to provide investors with information that is easier to use and more readily accessible, while retaining the comprehensive information that is currently available for those who desire it.

There are three components to the amendments. First, the Commission has amended Form N-1A to require that every fund prospectus contain a summary section at the beginning, consisting of specified key information about the fund, including investment objectives and strategies, risks, costs, and performance. Second, the Commission has amended certain disclosures required by ETFs registered as open-end management investment companies, which file on Form N-1A. Finally, the Commission has created a new option for funds to satisfy their prospectus delivery obligations. Under this option, a fund may send or give investors a document containing only this key information (a “Summary Prospectus”), provided that the full prospectus (the “statutory prospectus”) and other information is made available on the Internet, and in paper upon request. [3] Each of these components is described more fully below.

Amendments to Form N-1A

The amendments to Form N-1A require the statutory prospectus of every mutual fund to include a summary section at the front of the prospectus containing specified key information, presented in plain English, in a prescribed order. This concept is similar to the current risk/return summary. However, the amendments modify the format, content and specified order of information included in this section.

Format

The amendments generally require the summary information in the front of a statutory prospectus to be presented separately for each fund covered by a multiple fund prospectus; information for multiple funds may not be integrated, as was permitted in the risk/return summary. Information for multiple share classes of the same fund, however, may be integrated. In addition, where the information contained in any of items 6-8 of Form N-1A (purchase and sale of fund shares, tax information, and financial intermediary

compensation) is identical for all funds covered by a multiple fund prospectus, such information may be integrated. The integrated information must follow the separate individual fund summaries, and a statement directing readers to the section and page number containing the information must be included in each individual fund summary section at the location where such information would have appeared.

The Adopting Release suggests that the summary information should be presented in three to four pages per fund, but the amendments do not include a specific page limit.

Content

The amendments require the summary section of the statutory prospectus to contain specified information in a prescribed order, as set forth below. [\[4\]](#)

Investment objectives/goals (Item 2): The summary section must begin with a fund's investment objectives or goals, exactly as required in a fund's current risk/return summary.

Costs (fee table) (Item 3): The next required information is the fee table and example. These are similar to the current fee table and example, with several modifications in addition to their new location. [\[5\]](#) First, funds that offer discounts on front-end sales charges for volume purchases (breakpoint discounts) must include a brief narrative disclosure alerting investors to the availability of these discounts. Second, the parenthetical following the heading "Annual Fund Operating Expenses" has been revised. Instead of "Expenses that are deducted from fund assets," it must read "Expenses that you pay each year as a percentage of the value of your investment." Third, funds other than money market funds must include, immediately following the fee table example, their portfolio turnover rate for the most recent fiscal year, as a percentage of the average value of the portfolio, accompanied by a brief explanation of the effect of portfolio turnover on transaction costs and fund performance, and the potential adverse tax consequences.

Finally, the amendments modify the previous requirement in Form N-1A that a fund disclose gross operating expenses that do not reflect the effect of expense reimbursement or fee waiver arrangements. If a fund has an arrangement that will reduce its operating expenses for no less than one year from the effective date of the fund's registration statement, it may place two additional captions below the "Total Annual Fund Operating Expenses" caption. One caption should show the amount of the reimbursement or waiver, and the second should show the fund's total expenses net of the reimbursement or waiver. Funds disclosing these arrangements must also disclose the period for which the reimbursement or waiver arrangement is expected to continue, including the expected termination date, and briefly describe the circumstances under which the arrangement may be terminated. These arrangements may also be reflected in the fee table example, but only for periods for which the arrangement is expected to continue.

Investments, risks, and performance (Item 4): The next required item is principal investment strategies and risks. The required disclosure is the same as that currently required in the risk/return summary, including the risk/return bar chart and table illustrating the variability of returns and past performance. The amendments add a new requirement for funds that make updated performance information available on a Web site or at a toll-free or collect telephone number to include a statement explaining this and providing the Web site and/or telephone number.

Management (Item 5): The summary section must next include the name of each

investment adviser and sub-adviser of the fund, followed by the name, title, and length of service of each of the fund's portfolio managers. A fund is generally not required to identify a sub-adviser whose sole responsibility is day-to-day management of the fund's cash instruments, and a fund with three or more sub-advisers need not identify each sub-adviser, but only those advisers responsible for the management of a significant portion of the fund's net assets (generally 30% or more).

Purchase and sale of fund shares (Item 6): The summary section must next state the fund's minimum initial and subsequent investment requirements and that the fund's shares are redeemable, and identify the procedures for redeeming shares.

Tax information (Item 7): Next, the summary section must state, as applicable, that the fund intends to make distributions that may be taxed as ordinary income or capital gains, or that the fund intends to distribute tax-exempt income. A fund holding itself out as investing in securities generating tax-exempt income must provide, as applicable, a general statement that a portion of the fund's distributions may be subject to federal income tax.

Financial intermediary compensation (Item 8): Finally, the summary section must include the following – or similar – statement:

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.

A fund may omit this disclosure if neither the fund nor any of its related companies pay financial intermediaries for the sale of fund shares or related services.

Other Amendments to Form N-1A

The amendments eliminate the provisions in Form N-1A that permit a fund to omit detailed information about purchase and redemption procedures from the statutory prospectus and provide this information in a separate document that is incorporated into and delivered with the statutory prospectus. [\[6\]](#) A similar provision in the requirements for the Statement of Additional Information ("SAI") has also been eliminated.

Exchange-Traded Funds

In March 2008, the Commission proposed a new rule that would have permitted ETFs registered as open-end funds to begin operating without first obtaining exemptive relief under the Investment Company Act. The proposal contained several amendments to Form N-1A to better accommodate the use of the form by ETFs, with particular consideration for the needs of investors, including retail investors, who purchase ETF shares in secondary market transactions. The Commission has adopted several of these disclosure amendments in connection with the Summary Prospectus amendments, with certain changes to respond to issues raised by commenters on the ETF rule. [\[7\]](#) Subject to these modifications, ETFs may elect to use a Summary Prospectus to meet their delivery obligations.

Purchasing and redeeming shares, and associated costs: The amendments modify Form N-1A to eliminate the requirement that ETF prospectuses disclose information on how to

buy and redeem shares directly from the ETF. Instead, ETFs need only state the number of shares contained in a creation unit, that individual shares can only be bought or sold on the secondary market through a broker-dealer, and that shareholders may pay more than net asset value ("NAV") when they buy, and receive less than NAV when they sell, ETF shares because shares are bought and sold at market prices.

The amendments also permit ETFs to exclude from the fee table fees and expenses associated with the purchase and redemption of creation units, and instead to modify the narrative explanation preceding the example to state that investors may pay brokerage commissions that are not reflected in the example. [\[8\]](#)

Premium/discount information: The amendments require ETFs to disclose in their prospectuses information about the extent and frequency with which market prices of fund shares have tracked the fund's NAV. This information may be omitted from the prospectus if the ETF provides a free, publicly available Internet address that investors can use to obtain premium/discount information. For purposes of this information, "market price" means the closing price on the principal market on which the ETF shares trade, or within the range between the highest bid and lowest offer, if that price more accurately reflects the current market value of the fund's shares at the time the fund calculates its NAV.

New Delivery Option for Mutual Funds

The Commission has adopted amendments that essentially replace existing Rule 498, the voluntary fund profile rule, with a revised rule that permits a fund to satisfy its prospectus delivery obligation under Section 5(b)(2) of the Securities Act by providing a Summary Prospectus to investors, and making additional information, including the statutory prospectus, available on the Internet and in paper upon request. Revised Rule 498 specifies the criteria for satisfying statutory prospectus delivery requirements, the content of the Summary Prospectus, updating requirements for the Summary Prospectus, and requirements for the provision of additional information on the Internet.

Use of the Summary Prospectus to Satisfy Statutory Prospectus Delivery Requirements

Rule 498 provides that any obligation under Section 5(b)(2) of the Securities Act to have a statutory prospectus precede or accompany the carrying or delivery of a mutual fund security (in an offering registered on Form N-1A) is satisfied if: 1) a Summary Prospectus is provided no later than the time of the carrying or delivery of the fund security; [\[9\]](#) 2) the Summary Prospectus is not bound together with any other materials, with a specific exception for variable insurance contracts; [\[10\]](#) 3) the Summary Prospectus that is provided satisfies the rule's requirements with respect to content; and 4) the conditions set forth in the rule requiring the statutory prospectus and other information to be provided on the Internet are satisfied.

The rule also requires that, if a Summary Prospectus is being used to satisfy a fund's Section 5(b)(2) delivery obligations, the Summary Prospectus must have "greater prominence" than any materials, other than other Summary Prospectuses or statutory prospectuses, that accompany it. In addition, a fund must send a paper or email copy of the statutory prospectus or other information upon request, at no charge to the requestor, within three business days. These requirements are not a condition to reliance on the rule, however. Thus, a failure to meet the "greater prominence" requirement or to send additional materials upon request would not constitute a violation of Section 5(b)(2), but would be a violation of the rule.

Rule 498 also contains a provision that is similar to Section 2(a)(10)(a) of the Securities Act, which excludes from the definition of prospectus communications that accompany or are preceded by a statutory prospectus. Under the rule, a communication relating to an offering registered on Form N-1A provided after the effective date of the fund's registration statement (other than a prospectus permitted or required under Section 10 of the Securities Act) will not be deemed a prospectus if a Summary Prospectus was provided prior to or at the same time as such communication and the conditions of the rule relating to the availability of additional information on the Internet are satisfied. As a result of this provision, such communications would not be subject to liability under Section 12(a)(2) of the Securities Act. [\[11\]](#)

As with reliance for Section 5(b)(2) purposes, a fund relying on the delivery of a Summary Prospectus to assure that other communications are not deemed a prospectus must meet the "greater prominence" and delivery of additional information requirements. Failure to do so would constitute a violation of the rule, but would not render the communications prospectuses for purposes of Section 12(a)(2).

Contents of the Summary Prospectus

Rule 498 requires the Summary Prospectus to include the same information as the summary section of the statutory prospectus described above, in the same order. [\[12\]](#) Like the summary section, a Summary Prospectus may describe only a single fund, but may describe multiple share classes of the fund. The Summary Prospectus may not omit any of the required information or include additional information, except that it must contain certain information on a cover page or at the beginning of the Summary Prospectus, including: the fund's name and the share classes to which the Summary Prospectus relates; the exchange ticker symbol of the fund's securities (or symbols, in the case of a Summary Prospectus relating to multiple share classes); a statement identifying the document as a "Summary Prospectus"; and the approximate date of the Summary Prospectus's first use.

The cover page or beginning must also include a prescribed legend informing the reader that additional information is available online or by making a request by email or by telephone. [\[13\]](#) The legend must include an Internet address, toll-free or collect telephone number, and email address that investors can use to obtain the statutory prospectus and other information. [\[14\]](#) The Internet address at which the information is available may not be the Commission's EDGAR system, and the address must be specific enough to lead investors directly to the statutory prospectus and other required information, rather than to a home page or other section of a Web site on which the materials are posted. The Web site may be a central site with prominent links to each required document.

Updating Requirements

The Commission did not adopt the proposed requirement that certain information contained in the Summary Prospectus be provided as of the end of the most recent calendar quarter. Instead, the amendments to Form N-1A require that, if a fund makes updated performance information available on a Web site or at a toll-free or collect telephone number, the fund must include a statement explaining this and providing the Web site and/or telephone number. The Summary Prospectus itself must be updated with the same frequency as the fund's statutory prospectus.

Provision of the Statutory Prospectus, SAI and Shareholder Reports

To use the Summary Prospectus, a fund must meet certain conditions with respect to the availability of additional information.

Availability of Information on the Internet

The Summary Prospectus, statutory prospectus, SAI, and most recent annual and semi-annual reports to shareholders must be accessible, free of charge, at the Internet address specified on the cover page or at the beginning of the Summary Prospectus. The documents must be accessible on or before the time that the Summary Prospectus is provided. To satisfy the requirement that a statutory prospectus precede or accompany the carrying or delivery of a mutual fund security, the Summary Prospectus must remain available for at least 90 days after the security is delivered. To deem a communication not a prospectus under Section 2(a)(10) of the Securities Act, the Summary Prospectus must remain available for at least 90 days after the communication is sent or given.

The rule further requires information made available on the Internet to be presented in a format that:

- (1) is human-readable and capable of being printed on paper in human-readable format; [\[15\]](#)
- (2) permits a person accessing the statutory prospectus or SAI to move directly back and forth between each section heading in a table of contents of the document and the sections of the document that are referenced in that section heading; and
- (3) permits a person accessing the Summary Prospectus to move directly back and forth between a) each section of the Summary Prospectus and any section of the statutory prospectus or SAI that provides additional detail concerning information provided in the Summary Prospectus, or b) links located at both the beginning and end of the Summary Prospectus, or that remain continuously visible to persons accessing the Summary Prospectus, and tables of contents of both the statutory prospectus and SAI that themselves meet the requirements of (2).

The rule also requires that a person accessing the Web site be able to permanently retain, free of charge, an electronic version of each of the documents made available, in a format that is human-readable and capable of being printed on paper in human-readable format. [\[16\]](#) The retained versions of the statutory prospectus and SAI must also permit a reader to move back and forth between each section heading in a table of contents of the document and the sections of the document that are referenced in that section heading.

Compliance with these conditions is required to rely on the rule for purposes of Sections 5(b)(2) or 2(a)(10) of the Securities Act. However, the Commission recognizes that occasionally a fund may be out of compliance with these requirements despite its best efforts, due to system outages or other technological issues, natural disasters, acts of terrorism, or pandemic illnesses. Thus, the rule contains a safe harbor provision stating that the conditions regarding Internet availability of the required materials will be deemed to be met, notwithstanding that they are unavailable for a time in the manner required, provided that 1) the fund has reasonable procedures in place to ensure that the materials are available in the required manner, and 2) in the event of a problem, the fund takes prompt action to ensure that the materials become available as soon as practicable following the time at which the fund knows or reasonably should have known that the materials are not

available.

Provision of Information in Paper and by Email

The rule requires that a fund (or financial intermediary through which the fund may be purchased or sold) send, by U.S. first class mail or other reasonably prompt means, a paper copy of the fund's statutory prospectus, SAI, and most recent annual and semi-annual shareholder report to any person requesting such a copy, at no cost to such person, within three business days after receiving the request. The fund or financial intermediary would also be required to send an electronic copy of any such material by email, within three days of receiving a request for an electronic copy. This requirement may be met by sending a direct link to the document on the Internet, provided that 1) a current version of the document is accessible through that link for six months from the time the email is sent, and 2) the email explains how long the link will remain active and that if the recipient desires to retain a copy of the document, he or she should download and save it.

Incorporation by Reference

The rule permits a Summary Prospectus to incorporate by reference all of the information contained in the fund's statutory prospectus and SAI, as well as any information from the Fund's shareholder reports that the fund has incorporated by reference into its statutory prospectus. The rule provides that, for purposes of Sections 12(a)(2) and 17(a)(2) of the Securities Act, information incorporated by reference into a Summary Prospectus is deemed to be conveyed to a person not later than the time the person receives the Summary Prospectus.

The following conditions apply to incorporation by reference. First, information must be incorporated only by reference to the specific document in which it is contained, and not by reference to another document that incorporates the information by reference. Second, incorporation by reference is only permitted if a fund satisfies the conditions described above regarding the availability of the incorporated information on the Internet. Third, a legend in the Summary Prospectus must identify clearly the document from which the information is incorporated, including the date of the document. If only part of a document is incorporated by reference, the legend must identify the part by page, paragraph, caption or otherwise. The legend must also explain how the information that is incorporated by reference may be obtained.

Filing Requirements for the Summary Prospectus

The rule requires that each Summary Prospectus be filed with the Commission on EDGAR no later than the date that it is first used. The Summary Prospectus must be filed as part of the registration statement, but will not be deemed a part of the registration statement for purposes of Section 11 of the Securities Act. [\[17\]](#)

Compliance Date and Transition Period

The amendments are effective as of March 31, 2009. To allow a transition period after the effective date, all initial registration statements on Form N-1A, and all post-effective amendments that add a new series or are annual updates to effective registration statements on Form N-1A, filed on or after January 1, 2010 must comply with the amendments. A fund may elect to comply with the amendments at any time after the effective date. A fund may not rely on Rule 498 unless the fund is in compliance with the amendments to Form N-1A.

Post-effective amendments to existing registration statements filed to comply with the amendments must be filed under Securities Act Rule 485(a). The Adopting Release states that in appropriate circumstances, [18] the Commission will consider requests by existing funds to file post-effective amendments pursuant to Rule 485(b).

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endnotes

[1] See Enhanced Disclosure and New Prospectus Delivery Option for Registered Open-End Management Investment Companies, SEC Release Nos. 33-8998 and IC-28584 (Jan. 13, 2009) (“Adopting Release”), available at <http://www.sec.gov/rules/final/2009/33-8998.pdf>.

[2] See Exchange Traded Funds, SEC Release Nos. 33-8901 and IC-28193 (Mar. 11, 2008), available at <http://www.sec.gov/rules/proposed/2008/33-8901.pdf>.

[3] A Summary Prospectus meeting the requirements of the rule will be deemed a prospectus authorized under Section 10(b) of the Securities Act and Section 24(g) of the Investment Company Act of 1940.

[4] The Commission did not adopt the proposed requirement that the Summary Section contain a fund’s top ten portfolio holdings.

[5] In response to comments suggesting alternative terms to describe sales loads or Rule 12b-1 fees, the Adopting Release explains that the Commission concluded it would be more appropriate to consider such changes in the context of a full reconsideration of sales charges and Rule 12b-1.

[6] The Adopting Release indicates that this option is infrequently used, and that it seems unnecessary because under the amendments, a fund may provide a Summary Prospectus, along with any additional sales materials, including a document describing purchase and redemption procedures.

[7] The Adopting Release explains that several of the proposed ETF disclosure amendments were not adopted, based on the suggestions of commenters. These include the proposed requirements that ETFs include the disclosure of market price returns in addition to returns based on NAV, and that index-based ETFs compare their performance to their underlying index rather than a benchmark index.

[8] These changes do not apply to funds that issue creation units of less than 25,000 shares.

[9] A fund may rely on existing Commission guidance, which typically requires affirmative consent, to provide the Summary Prospectus by electronic means.

[10] Specifically, a Summary Prospectus for a fund that is available as an investment option in a variable annuity or variable life insurance contract may be bound together with the statutory prospectus for the contract, and Summary Prospectuses or statutory

prospectuses for other investment options available in the contract, provided that 1) all of the funds to which the prospectuses that are bound together relate are available to the person to whom such documents are provided, and 2) a table of contents identifying each prospectus that is bound together, and the page number on which it is found, is included at the beginning of the bound materials.

[\[11\]](#) Such communications would, however, be subject to the general antifraud provisions of the federal securities laws; specifically, Section 17(a) of the Securities Act, Section 10(b) of the Securities Exchange Act of 1934, and Section 34(b) of the Investment Company Act.

[\[12\]](#) As adopted, the rule explicitly states that information in the Summary Prospectus must be the same as information in the summary section of the statutory prospectus. The Adopting Release explains that this provision is intended to clarify that a fund may not provide different, such as more or less expansive, information in its Summary Prospectus. Further, if a fund relies on Rule 497 to “sticker” its statutory prospectus, those changes must also be reflected in its Summary Prospectus, either by means of a “sticker” or amendment. Finally, the Adopting Release points to this provision in addressing some commenters’ concerns that Summary Prospectuses are not subject to liability under Section 11 of the Securities Act. The Adopting Release explains that because the information is identical to that contained in the statutory prospectus, the information in the Summary Prospectus is subject to Section 11 liability by virtue of its inclusion in the statutory prospectus.

[\[13\]](#) Where applicable, the legend may include a statement that the Summary Prospectus is intended for use in connection with a defined contribution plan that meets the requirements of certain provisions of the Internal Revenue Code, and is not intended for use by other investors.

[\[14\]](#) The legend may indicate that this information is available from a financial intermediary through which shares of the fund may be purchased or sold.

[\[15\]](#) The rule also requires that this information be made available in a format or formats that are convenient for reading online and printing on paper. Failure to provide such a format is a violation of the rule, but is not a condition of reliance on the rule for purposes of Sections 5(b)(2) or 2(a)(10) of the Securities Act. The Adopting Release acknowledges the importance of objective standards, such as “human readable,” for purposes of compliance with these sections.

[\[16\]](#) The documents must also be available for saving in a format or formats that are convenient for reading online and printing on paper, but this requirement is not a condition to reliance on the rule for purposes of Sections 5(b)(2) or 2(a)(10) of the Securities Act.

[\[17\]](#) See *supra* note 12.

[\[18\]](#) The Adopting Release provides as an example a situation where a fund complex has previously filed post-effective amendments under Rule 485(a) for other funds to comply with the new requirements; in such a case, the staff may determine not to review additional filings by the same complex.

abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice.