Enhanced Government Income Fund
Form 497
October 27, 2005
PROSPECTUS

12,000,000 Shares

Enhanced Government Fund, Inc.

Common Stock

Enhanced Government Fund, Inc. is a newly organized, diversified, closed-end fund. The Fund s investment objective is to provide stockholders with current income and gains. No assurance can be given that the Fund s investment objective will be achieved. The Fund has an interval fund structure, pursuant to which the Fund will conduct annual repurchase offers for between 5% and 25% of the Fund s outstanding shares.

The Fund seeks to achieve its investment objective by investing primarily in a portfolio of U.S. Government securities and U.S. Government Agency securities, including U.S. Government mortgage-backed securities, that pay interest in an attempt to generate current income, and by employing a strategy of writing (selling) call options on individual or baskets of U.S. Government securities, U.S. Government Agency securities or other debt securities held by the Fund in an attempt to generate gains from option premiums (the Option Strategy).

(continued on following page)

Investing in the Fund s common stock involves certain risks and should not constitute a complete investment program. Risks are described in the Risk Factors and Special Considerations section beginning on page 13 of this prospectus.

	Per Share	Total(3)
Public offering price	$ 20.00	$240,000,000
Sales load(1)	$ .90	$10,800,000
Proceeds, before expenses, to the Fund(2)	$ 19.10	$229,200,000

(1) The Fund has agreed to pay the underwriters $.00667 per share of common stock as a partial reimbursement of expenses incurred in connection with the offering. The Fund s investment adviser has agreed to pay additional compensation to Merrill Lynch, Pierce, Fenner & Smith Incorporated for acting as lead underwriter and for after-market services. See Underwriting.

(2) The Fund s investment adviser has agreed to pay all organizational expenses of the Fund. The investment adviser also has agreed to pay the amount by which the offering costs of the Fund (other than the underwriting discount) exceeds $.04 per share of common stock. The estimated offering expenses to be incurred by the Fund are $375,000.

(3) The underwriters also may purchase up to an additional 1,800,000 shares at the public offering price, less the sales load, within 45 days from the date of this prospectus to cover overallotments. If all such shares are purchased, the total public offering price will be $276,000,000, the total sales load will be $12,420,000 and the total proceeds, before expenses, to the Fund will be $263,580,000.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The shares will be ready for delivery on or about October 31, 2005.

Merrill Lynch & Co. **Citigroup**

Advest, Inc.

Fixed Income Securities, L.P.

J.J.B. Hilliard, W.L. Lyons, Inc.

The date of this prospectus is October 26, 2005.

(continued from previous page)

Under normal market conditions and after the initial investment period of up to approximately three months following completion of this offering, the Fund will invest at least 80% of the value of its net assets (including assets acquired with the proceeds from the sale of any preferred stock), plus the amount of any outstanding debt securities or borrowings for investment purposes, in U.S. Government securities and U.S. Government Agency securities, including U.S. Government mortgage-backed securities. The Fund may also invest up to 20% of its net assets in non-U.S. Government debt securities of foreign or domestic issuers, including commercial paper, notes, corporate bonds, debentures, asset-backed securities, mortgage-backed securities, corporate loans, sovereign debt securities and money market securities, that are rated in one of the four highest rating categories by at least one of the nationally recognized statistical rating organizations (including Baa or better by Moody s Investors Service, Inc. or BBB or better by Standard & Poor s, a division of The McGraw-Hill Companies, Inc., or Fitch Ratings) or, if unrated, are considered by the Fund s investment adviser to be of comparable quality. Securities rated in any of the four highest rating categories are known as investment grade securities. As part of its Option Strategy, the Fund may also write (sell) call options on these other debt securities.

Under the Option Strategy, the Fund will write call options on individual U.S. Government securities, U.S. Government Agency securities or other debt securities or baskets of such securities on a continuous basis such that the value of the securities underlying such options does not exceed the value of the Fund s portfolio. While the Fund will receive premiums under the Option Strategy, the Fund gives up any potential increase in the value of the securities above the exercise price specified in the written call option through the expiration date of the call option. The Fund also may use other derivative strategies involving call and put options, futures and forward contracts, swap agreements, options on swaps, short sales and other derivative instruments in an attempt to enhance return or to hedge against market and other risks in the portfolio.

Although the Fund has no present intention to use leverage, it may in the future leverage its portfolio through borrowings, the issuance of debt securities, the issuance of preferred stock or a combination thereof. See Other Investment Policies Leverage. The Fund may enter into derivatives transactions that in certain circumstances may produce effects similar to leverage. See Risk Factors and Special Considerations Other Portfolio Strategies.

Because the Fund is newly organized, its shares of common stock have no history of public trading. Shares of common stock of closed-end investment companies frequently trade at a price lower than their net asset value. This is commonly referred to as trading at a discount. The risk may be greater for investors expecting to sell their shares in a relatively short period after completion of the public offering. The Fund s shares of common stock have been approved for listing on the New York Stock Exchange under the symbol EGF, subject to offical notice of issuance.

This prospectus contains information you should know before investing, including information about risks. Please read it before you invest and keep it for future reference. Copies of the Fund s semi-annual and annual reports may be obtained without charge by writing to the Fund at its address at 800 Scudders Mill Road, Plainsboro, New Jersey 08536, or by calling the Fund at (800) 543-6217. Copies of the Fund s semi-annual and annual reports may also be obtained without charge at www.mutualfunds.ml.com. In addition, the Securities and Exchange Commission maintains a website (http://www.sec.gov) that contains the annual and semi-annual reports and other information regarding registrants that file electronically with the Securities and Exchange Commission.

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Information about the Fund can be reviewed and copied at the Securities and Exchange Commission s Public Reference Room in Washington, D.C. Call 1-202-551-8090 for information on the operation of the public reference room. This information is also available on the Securities and Exchange Commission s Internet site at http://www.sec.gov and copies may be obtained upon payment of a duplicating fee by writing the Public Reference Section of the Commission, Washington, D.C. 20549-0102.

You should rely only on the information contained in this prospectus. We have not, and the underwriters have not, authorized any other person to provide you with different information. If anyone provides you with different or inconsistent information, you should not rely on it. We are not, and the underwriters are not, making an offer to sell these securities in any jurisdiction where the offer or sale is not permitted. You should assume that the information appearing in this prospectus is accurate only as of the date on the front cover of this prospectus. Our business, financial condition, results of operations and prospects may have changed since that date.

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PROSPECTUS SUMMARY

This summary is qualified in its entirety by reference to the detailed information included in this prospectus.

The Fund Enhanced Government Fund, Inc. is a newly organized, diversified, closed-end fund. The Fund has an interval fund structure, pursuant to which the Fund will conduct, subject to applicable Maryland law, annual repurchase offers for between 5% and 25% of the Fund s outstanding shares. See Annual Repurchases of Fund Shares for more information about the interval fund structure.

The Offering

The Fund is offering 12,000,000 shares of common stock at an initial offering price of $20.00 per share through a group of underwriters led by Merrill Lynch, Pierce, Fenner & Smith Incorporated (Merrill Lynch). You must purchase at least 100 shares of common stock. The underwriters may purchase up to an additional 1,800,000 shares of common stock within 45 days from the date of this prospectus to cover overallotments, if any.

Investment Objective and Policies

The Fund s investment objective is to provide stockholders with current income and gains. No assurance can be given that the Fund s investment objective will be achieved.

The Fund seeks to achieve its investment objective by investing primarily in a portfolio of U.S. Government securities and U.S. Government Agency securities, including U.S. Government mortgage-backed securities, that pay interest in an attempt to generate current income and by employing a strategy of writing (selling) call options on individual or baskets of U.S. Government or U.S. Government Agency securities or other debt securities held by the Fund in an attempt to generate gains from option premiums (the Option Strategy).

Under normal market conditions and after the initial investment period of up to approximately three months following completion of this offering, the Fund will invest at least 80% of the value of its net assets (including assets acquired with the proceeds from the sale of any preferred stock), plus the amount of any outstanding debt securities or borrowings for investment purposes, in U.S. Government securities and U.S. Government Agency securities, including U.S. Government mortgage-backed securities. U.S. Government securities are debt securities issued and/or guaranteed as to principal and interest by the U.S. Government that are supported by the full faith and credit of the United States. U.S. Government Agency securities, as used in this prospectus, include debt securities issued and/or guaranteed as to principal and interest by U.S. Government agencies, U.S. Government sponsored enterprises and U.S. Government instrumentalities that are not direct obligations of the United States. These securities may not be backed by the full faith and credit of the United States. U.S. Government-sponsored enterprises and instrumentalities are not agencies of the U.S. Government. See Investment Objective and Policies U.S. Government Securities and U.S. Government Agency Securities. In selecting portfolio securities, Fund Asset Management, L.P., the Fund s investment adviser (the Investment Adviser), will consider the relative yield of different types of U.S. Government securities and U.S. Government Agency securities and its assessment of future interest rate patterns.

The Fund may also invest up to 20% of its net assets in non-U.S. Government debt securities of foreign or domestic issuers, including commercial paper, notes, corporate bonds, debentures, asset-backed securities, mortgage-backed securities, corporate loans, sovereign debt securities and money market securities that are rated in one of the four highest rating categories by at least one of the nationally recognized statistical rating organizations (including Baa or better by Moody s Investors Service, Inc. (Moody s) or BBB or better by Standard & Poor s, a division of The McGraw-Hill Companies, Inc. (S&P), or Fitch Ratings (Fitch)) or, if unrated, are considered by the Fund s Investment Adviser to be of comparable quality (referred to herein as other debt securities). As part of its Option Strategy, the Fund may also write (sell) call options on these other debt securities.

The Fund is not limited as to the maturities of its portfolio investments and may take full advantage of the entire range of maturities offered by U.S. Government securities, U.S. Government Agency securities and other debt securities. Initially, it is expected that the Fund will target an average maturity of between three and ten years (for mortgage-backed securities, maturity will be considered to be the average remaining life based on certain prepayment assumptions). The Investment Adviser may adjust the average maturity of the Fund s portfolio from time to time, depending on its assessment of the relative yields available on securities of different maturities and its assessment of future interest rate patterns.

Most of the options written by the Fund will be traded over-the-counter, although the Fund may utilize exchange-traded options as well. In general, the Fund will primarily write (sell) call options that are European style, meaning that the options may be exercised only on the expiration date. However, the Fund may from time to time write call options that are American style, meaning that the options may be exercised at any point up to and including the expiration date.

The Fund will generally write (sell) call options that are out-of-the-money or at-the-money at the time of sale. Out-of-the-money call options are options with an exercise price that is above the principal value of the U.S. Government securities, U.S. Government Agency securities or other debt securities at the time of sale whereas at-the-money call options are options with an exercise price that is equal to the principal value of the U.S. Government securities, U.S. Government Agency securities or other debt securities at the time of sale. In addition to providing possible gains through premiums, out-of-the-money call options allow the Fund to potentially benefit from appreciation in the U.S. Government securities, U.S. Government Agency securities or other debt securities held by the Fund with respect to which the option was written, up to the exercise price. The Fund also reserves the right to sell call options that are in-the-money (*i.e.*, those with an exercise price below the principal value of the security at the time of sale). When the price of the security upon which a call option is written rises, call options that were out-of-the-money when written may become in-the-money (*i.e.,* the principal value of the security rises above the exercise price of the option), thereby increasing the likelihood that the options will be exercised and the Fund will be forced to sell the security at the exercise price upon the purchaser s exercise of the option.

Initially, the Fund expects that it will primarily write call options whose terms to expiration range from one to three months. The Fund reserves the right to sell call options of both longer and shorter terms.

The Investment Adviser will attempt to maintain for the Fund written call options positions on U.S. Government securities, U.S. Government Agency securities or other debt securities whose price movements, taken in the aggregate, are correlated with the price movements of the U.S. Government securities, U.S. Government Agency securities and other debt securities held in the Fund s portfolio. In doing so, the Investment Adviser will consider data relating to the Fund s fixed income holdings, including interest rates, maturity and coupon rate. The Fund cannot guarantee that the Option Strategy will be effective. The Fund anticipates that initially it will write (sell) call options on a substantial portion of the U.S. Government securities, U.S. Government Agency securities and other debt securities held in its portfolio. See Risk Factors and Special Considerations Risks Associated with Writing Call Options.

Credit Quality. The Fund may invest in non-U.S. Government debt securities that are rated in one of the four highest rating categories by at least one of the nationally recognized statistical rating organizations (Baa or higher by Moody s, BBB or higher by S&P or BBB or higher by Fitch) or, if unrated, are considered by the Investment Adviser to be of comparable quality. Securities rated in any of the four highest rating categories are known as investment grade.

Foreign Securities. The Fund may invest up to 20% of its net assets in debt securities of issuers domiciled outside the United States.

Other Portfolio Strategies. The Fund may use a variety of other portfolio strategies both to seek to increase the return of the Fund and to seek to hedge, or protect, its exposure to interest rate movements and movements in the securities markets. These strategies include the use of derivatives, such as indexed securities, inverse securities, interest rate transactions (including interest rate swaps), credit default swaps, total return swaps, options on swaps, options, futures, options on futures, short sales and foreign exchange transactions.

The Fund s hedging transactions are designed to reduce volatility, but may come at some cost. For example, the Fund may try to limit its risk of loss from a decline in price of a portfolio security by purchasing a put option. However, the Fund must pay for the option, and the price of the security may not in fact drop. In large part, the success of the Fund s hedging activities depends on the Investment Adviser s ability to forecast movements in securities prices and interest rates. The strategies used by the Fund in seeking to enhance its return may be riskier and have more speculative aspects than its hedging strategies. The Fund is not required to use derivatives to seek to increase return or to seek to hedge its portfolio and may choose not to do so. The Fund cannot guarantee that any strategies it uses will work.

Risk Factors

Set forth below is a summary of the main risks of investing in the Fund s common stock. For a more detailed description of the main risks as well as certain other risks associated with investing in the Fund s common stock, see Risk Factors and Special Considerations.

Liquidity and Market Price of Shares. The Fund is newly organized and has no operating history or history of public trading. Shares of closed-end funds that trade in a secondary market frequently trade at a market price that is below their net asset value (commonly referred to as trading at a discount).

Issuer Risk; Market Risk; Selection Risk. Issuer risk is the risk that the value of securities may decline for a number of reasons directly related to the issuer or borrower. Market risk is the risk that the market will go down in value, including the possibility that the market will go down sharply and unpredictably. Selection risk is the risk that the securities that Fund management selects will underperform the relevant market indices or other funds with similar investment objectives and strategies.

Interest Rate Risk. The Fund s investments in U.S. Government securities, U.S. Government Agency securities and other debt securities are subject to interest rate risk. This is the risk that the value of such securities may fall when interest rates rise and rise when interest rates decline. Prices of longer term securities generally change more in response to interest rate changes than prices of shorter term securities.

Risks Associated with U.S. Government Agency Securities. U.S. Government Agency securities including securities issued by U.S. Government-sponsored enterprises and instrumentalities are not direct obligations of the United States and may not be backed by the full faith and credit of the United States. The Federal National Mortgage Association and the Federal Home Loan Mortgage Association have each been subject to investigations by federal regulators over certain accounting matters. Such investigations, and any resulting restatements of financial statements, may adversely affect the credit quality, availability or investment character of the securities issued or guaranteed by those entities.

Risks Associated with Writing Call Options. There are various risks associated with the Option Strategy. The purchaser of an option written (sold) by the Fund has the right to purchase the security underlying the option at the exercise price up to and including the expiration date of the option. Therefore, as the writer of a call option, the Fund forgoes, during the term of the option, the opportunity to profit from increases in the market value of the underlying securities held by the Fund with respect to which the option was written above the sum of the premium and the exercise price of the call. However, the Fund has retained the risk of loss (net of premiums received) should the price of the Fund s portfolio securities decline. Consequently, as a result of the Option Strategy, the net asset value of the Fund may tend to decline over time.

A decision as to whether, when and how to use options involves the exercise of skill and judgment and even a well conceived transaction may be unsuccessful to some degree because of market developments or unexpected events.

Risks of Investing in Mortgage-backed Securities. Mortgage-backed securities represent the right to receive a portion of principal and/or interest payments made on a pool of residential or commercial mortgage loans. When interest rates fall, borrowers may refinance or otherwise repay principal on their mortgages earlier than scheduled. When this happens, certain types of mortgage-backed securities will be paid off more quickly than originally anticipated and the Fund has to invest the proceeds in securities with lower yields. This risk is known as prepayment risk. When interest rates rise, certain types of mortgage-backed securities will be paid off more slowly than originally anticipated and the value of these securities will fall. This risk is known as extension risk.

Credit Risk. Credit risk is the risk that the issuer will be unable to pay the interest or principal when due. The degree of credit risk depends on both the financial condition of the issuer and the terms of the obligation.

Call and Redemption Risk. A bond s issuer may call a bond for redemption before it matures. If this happens to a bond the Fund holds, the Fund may lose income and may have to invest the proceeds in bonds with lower yields.

Income Risk. The income shareholders receive from the Fund is based primarily on the interest it earns from its investments as well as the gains the Fund receives from writing call options and selling portfolio securities, each of which can vary widely over the short and long term.

Other Portfolio Strategies. In addition to writing (selling) call options on U.S. Government securities, U.S. Government Agency securities and other debt securities held by the Fund, the Fund may engage in various other portfolio strategies both to seek to increase the return of the Fund and to seek to hedge its portfolio against adverse effects from movements in interest rates and in the securities markets. These additional strategies include the use of derivative instruments, such as purchased call options, purchased or written put options, indexed securities, inverse securities, options, futures, options on futures, interest rate transactions, credit default swaps, interest rate swaps, options on swaps, total return swaps, short sales and foreign exchange transactions. Such strategies subject the Fund to the risk that, if the Investment Adviser incorrectly forecasts market values, interest rates or other applicable factors, the Fund s performance could suffer. Certain of these strategies such as inverse securities, credit default swaps, interest rate swaps, total return swaps and short sales may provide investment leverage to the Fund s portfolio and may result in many of the same risks of leverage to the holders of the Fund s common stock as discussed below under Use of Leverage by the Fund. The Fund is not required to use derivatives or other portfolio strategies to seek to increase return or to seek to hedge its portfolio and may choose not to do so. No assurance can be given that the Fund s portfolio strategies will be effective. Some of the derivative strategies that the Fund may use to increase its return are riskier than its hedging transactions and have speculative characteristics. Such strategies do not attempt to limit the Fund s risk of loss.

General Risks Related to Derivatives. Derivatives are financial contracts or instruments whose value depends on, or is derived from, the value of an underlying

asset, reference rate or index (or relationship between two indices). The Fund also may have exposure to derivatives through investment in credit linked notes, credit linked trust certificates and other securities issued by special purpose or structured vehicles. The Fund may use derivatives as a substitute for taking a position in an underlying security or other asset, as part of a strategy designed to reduce exposure to other risks, such as interest rate risk. The Fund s use of derivative instruments involves risks different from, and possibly greater than, the risks associated with investing directly in securities and other traditional investments.

Risks of Investing in Foreign Securities. The Fund may invest up to 20% of its net assets in debt securities of foreign issuers. Such investments involve risks including fluctuation in foreign interest rates, future foreign political and economic developments and the possible imposition of exchange control or other governmental laws or regulations.

Annual Repurchases of Fund Shares. The Fund has an interval fund structure, pursuant to which the Fund will conduct, subject to applicable Maryland law, annual repurchase offers for between 5% and 25% of the Fund s outstanding shares. These required annual repurchases are likely to decrease the overall size of the Fund, which could over time: (i) harm the Fund s investment performance by limiting the extent to which the Fund may invest in illiquid securities; (ii) increase the Fund s expense ratio as the Fund s assets decrease; (iii) threaten the Fund s continued listing of its shares of common stock on the New York Stock Exchange and, consequently, the liquidity of its shares; and (iv) jeopardize the Fund s viability and continued existence. In addition, no assurance can be given that the annual repurchase offer will reduce any discount at which Fund shares trade or that the Fund will purchase all of the shares tendered by Fund shareholders during an annual repurchase offer period. See Annual Repurchases of Fund Shares for more information regarding the risks associated with the interval fund structure and annual repurchases of Fund shares.

Use of Leverage by the Fund

Although the Fund has no present intention to use leverage, it may in the future leverage its portfolio through borrowings, the issuance of debt securities, the issuance of preferred stock or a combination thereof. The Fund may borrow money and issue debt securities in amounts up to $33^1/3$ %, and may issue shares of preferred stock in amounts up to 50%, of the value of its total assets to finance additional investments. No assurance can be given that the Fund will not leverage its portfolio.
The proceeds from any leverage will be invested in accordance with the investment objectives of the Fund. The expenses of any leverage will be borne by the Fund and will reduce the net asset value of its common stock. During periods when the Fund has borrowings, debt securities or preferred stock outstanding, the Fund will pay fees to the Investment Adviser for its services that are higher than if the Fund did not borrow or issue debt securities or preferred stock, because the fees will be calculated on the basis of an aggregate of: (i) the Fund s average daily net assets (including proceeds received from the sale of any preferred stock) and (ii) the proceeds of any outstanding debt securities or borrowings used for leverage.

In addition, in the event the Fund uses leverage, it may not declare any cash dividend or other distribution upon any class of its capital stock, including its common stock, or purchase any such capital stock, unless certain asset coverage tests are satisfied. See Dividends and Distributions.
Risks of Leverage. The use of leverage involves risks, which can be significant. These risks include greater volatility in the Fund s net asset value, fluctuations in dividends and other distributions paid by the Fund and the market price of the Fund s common stock, the possibility that the value of the assets acquired with such borrowing will decrease although the Fund s liability is fixed and increased operating costs which may reduce the Fund s total return. So long as the Fund uses leverage, it may be required to sell investments in order to make interest or dividend payments on borrowings or preferred stock used for leverage when it may be disadvantageous to do so. Finally, if the Fund uses leverage and certain asset coverage requirements (as a result of market fluctuations or otherwise) are not satisfied, the Fund may be required to sell a portion of its investments to repay its borrowings or redeem some or all of its debt securities or preferred stock when it may be disadvantageous to do so. No assurance can be given that any leverage strategy used by the Fund will be successful. See Risk Factors and Special Considerations Leverage Risk.

Investment Adviser

Fund Asset Management, L.P., the Investment Adviser, provides investment advisory and management services to the Fund. For its services, the Fund pays the Investment Adviser a monthly fee at the annual rate of 0.85% of the aggregate of: (i) the Fund s average daily net assets (including proceeds from the sale of any preferred stock) and (ii) the proceeds of any outstanding debt securities or borrowings used for leverage.

Dividends and Distributions

The Fund intends to distribute dividends from its net investment income monthly, and net realized capital gains, if any, at least annually. The Fund expects that it will commence paying dividends within 90 days of the date of this prospectus. Currently, in order to maintain a more stable level of monthly dividend distributions, the Fund intends to pay out less than all of its net investment income or pay out accumulated undistributed income in addition to current net investment income. As a result, the dividend paid by the Fund to holders of common stock for any particular period may be more or less than the amount of net investment income earned by the Fund during such period. The Fund is not required to attempt to maintain a more stable level of distributions to stockholders and may choose not do so.

There is a possibility that the Fund may make total distributions during a calendar or fiscal year in an amount that exceeds the Fund s net investment income and net realized capital gains for the relevant fiscal year. In such situations, the amount by which the Fund s total distributions exceed net investment income and net realized capital gains would generally be treated as a tax-free return of capital up to the amount of a stockholder s tax basis in his or her shares, with any amounts exceeding such basis treated as gain from the sale of shares.

Section 19(a) of the Investment Company Act of 1940, as amended, and Rule 19a-1 thereunder require the Fund to provide a written statement accompanying payment

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from any source other than the Fund s income that adequately discloses the source or sources of such payment. Thus, if the Fund s capital were the source of a distribution, and the payment amounted to a return of capital, the Fund would be required to provide written notice to that effect. Nevertheless, stockholders who periodically receive distributions from the Fund may be under the impression that such payments are made from the Fund s income when, in fact, they are not. Accordingly, stockholders should carefully read any written disclosure accompanying a distribution and should not assume that the source of payment is the Fund s income

Automatic Dividend Reinvestment

Plan Dividends and capital gains distributions generally are used to purchase additional shares of the Fund s common stock. However, an investor can choose to receive dividends and distributions in cash. Stockholders whose shares of common stock are held in the name of a broker or nominee should contact the broker or nominee to confirm whether the broker or nominee will permit them to participate in the automatic dividend reinvestment plan.

Listing

Currently, there is no public market for the Fund s common stock. However, the Fund s shares of common stock have been approved for listing on the New York Stock Exchange under the symbol EGF, subject to official notice of issuance.

Federal Income Taxation

Distributions from the Fund s net investment income will generally be treated as dividends to the extent of the Fund s current or accumulated earnings and profits, as calculated for Federal income tax purposes. Except in the case of distributions of net capital gains, such dividends generally will be taxable as ordinary income to stockholders. Due to the nature of the Fund s investments, dividends from the Fund s net investment income will generally not be eligible for treatment as qualified dividend income taxed at the reduced rate applicable to long-term capital gains. Distributions of net capital gain that are designated by the Fund as capital gain dividends will be treated as long-term capital gains in the hands of stockholders receiving such distribution. See Taxes.

The Option Strategy and certain other transactions entered into by the Fund are subject to special tax rules that may, among other things, (i) affect the character of gains and losses realized, (ii) disallow, suspend or otherwise limit the allowance of certain losses or deductions and (iii) accelerate the recognition of income without a corresponding receipt of cash (with which to make the necessary distributions to satisfy distribution requirements applicable to regulated investment companies). Operation of these rules could, therefore, affect the character, amount and timing of distributions to stockholders. Some of the Fund s call option premiums will be subject to rules requiring the Fund to mark to market certain types of positions (*i.e.,* treat them as sold on the last day of the taxable year), and may result in the recognition of income without a corresponding receipt of cash. The Fund intends to monitor its transactions, to make appropriate tax elections and to make appropriate entries in its books and records to lessen the effect of these tax rules and avoid any possible disqualification for the favorable tax treatment afforded regulated investment companies. See Taxes.

RISK FACTORS AND SPECIAL CONSIDERATIONS

An investment in the Fund s common stock may be speculative in that it involves a high degree of risk and should not constitute a complete investment program.

Set forth below are the main risks of investing in the Fund s common stock.

Liquidity and Market Price of Shares. The Fund is newly organized and has no operating history or history of public trading.

Shares of closed-end funds that trade in a secondary market frequently trade at a market price that is below their net asset value. This is commonly referred to as trading at a discount. The risk may be greater for investors expecting to sell their shares in a relatively short period after completion of the public offering. Accordingly, the Fund is designed primarily for long term investors and should not be considered a vehicle for trading purposes. Net asset value will be reduced following the offering by the underwriting discount and the amount of offering expenses paid by the Fund.

Issuer Risk; Market Risk; Selection Risk. Issuer risk is the risk that the value of securities may decline for a number of reasons directly related to the issuer or borrower. Market risk is the risk that one or more markets in which the Fund invests will go down in value, including the possibility that the market will go down sharply and unpredictably. Selection risk is the risk that the securities that the Investment Adviser selects will underperform the markets, the relevant indices or other funds with similar investment objectives and investment strategies.

Interest Rate Risk. Interest rate risk is the risk that prices of bonds generally increase when interest rates decline and decrease when interest rates increase. Prices of longer term securities generally change more in response to interest rate changes than prices of shorter term securities.

Risk Associated with U.S. Government Agency Securities. U.S. Government Agency securities, including securities issued by U.S. Government-sponsored enterprises and instrumentalities are not direct obligations of the United States and may not be backed by the full faith and credit of the United States. Certain U.S. Government-sponsored enterprises (such as the Government National Mortgage Association) are backed by the full faith and credit of the U.S. Government. However, other government-sponsored enterprises (such as the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation and the Federal Home Loan Banks) are not backed by the full faith and credit of the U.S. Government. Such enterprises are supported only by the discretionary authority of the U.S. Government to purchase the enterprises obligations, and therefore are subject to increased credit risk. The Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation have each been the subject of investigations by federal regulators over certain accounting matters. Such investigations, and any resulting restatements of financial statements, may adversely affect the credit quality, availability or investment character of the securities issued or guaranteed by these entities. Congress has been considering legislation that would affect the regulation of these institutions. To the extent that legislation or federal regulators impose additional requirements or restrictions with respect to the ability of such institutions to issue or guarantee securities, particularly in connection with highly leveraged transactions, the availability of government agency-issued or -guaranteed securities for investment may be adversely affected. Further, such legislation or regulation could depress the market value of government agency-issued or -guaranteed securities.

Risks Associated with Writing Call Options. There are various risks associated with the Option Strategy. The purchaser of an option written (sold) by the Fund has the right to purchase the security underlying the option at the exercise price up to and including the expiration date of the option. Therefore, as the writer of a call option, the Fund forgoes, during the term of the option, the opportunity to profit from increases in the market value of the underlying securities held by the Fund with respect to which the option was written above the sum of the premium and the exercise price of the call. However the Fund has retained the risk of loss (net of premiums received) should the price of the Fund s portfolio securities decline. Consequently, as a result of the Option Strategy, the net asset value of the Fund may tend to decline over time.

A decision as to whether, when and how to use options involves the exercise of skill and judgment and even a well conceived transaction may be unsuccessful to some degree because of market developments or unexpected events.

Risks of Investing in Mortgage-Backed Securities. Mortgage-backed securities represent the right to receive a portion of principal and/or interest payments made on a pool of residential or commercial mortgage loans. When interest rates fall, borrowers may refinance or otherwise repay principal on their mortgages earlier than scheduled. When this happens, certain types of mortgage-backed securities will be paid off more quickly than originally anticipated and the Fund has to invest the proceeds in securities with lower yields. This risk is known as prepayment risk. When interest rates rise, certain types of mortgage-backed securities will be paid off more slowly than originally anticipated and the value of these securities will fall. This risk is known as extension risk.

Because of prepayment risk and extension risk, mortgage-backed securities react differently to changes in interest rates than other fixed income securities. Small movements in interest rates (both increases and decreases) may quickly and significantly reduce the value of certain mortgage-backed securities.

Mortgage-backed securities are issued by Federal government agencies such as the Government National Mortgage Association (Ginnie Mae), the Federal Home Loan Mortgage Corporation (Freddie Mac) or the Federal National Mortgage Association (Fannie Mae). Principal and interest payments on mortgage-backed securities issued by Federal government agencies are guaranteed by either the Federal government or the government agency. Such securities have very little credit risk, but may be subject to substantial interest rate risks.

Mortgage-backed securities may be either pass-through securities or collateralized mortgage obligations (CMOs). Pass-through securities represent a right to receive principal and interest payments collected on a pool of mortgages, which are passed through to security holders (less servicing costs). CMOs are created by dividing the principal and interest payments collected on a pool of mortgages into several revenue streams (tranches) with different priority rights to portions of the underlying mortgage payments. Certain CMO tranches may represent a right to receive interest only (IOs), principal only (POs) or an amount that remains after other floating-rate tranches are paid (an inverse floater). These securities are frequently referred to as mortgage derivatives and may be extremely sensitive to changes in interest rates. If the Fund invests in CMO tranches issued by government agencies and interest rates move in a manner not anticipated by Fund management, it is possible that the Fund could lose all or substantially all of its investment.

Prepayment Risk. The risk that certain obligations will be paid off by the obligor more quickly than anticipated. In this event, the Fund may be required to invest the proceeds in securities with lower yields.

Extension Risk. The risk that certain obligations will be paid off more slowly by the obligor than anticipated causing the value of these securities to fall.

Credit Risk. Credit risk is the risk that the issuer will be unable to pay the interest or principal when due. Changes in an issuer s credit rating or the market s perception of an issuer s creditworthiness may also affect the value of the Fund s investment in the issuer. The degree of credit risk depends on both the financial condition of the issuer and the terms of the obligation.

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Obligations issued or guaranteed by the U.S. Government are considered to have minimal credit risk. Obligations issued or guaranteed by U.S. Government agencies or U.S. Government-sponsored enterprises and instrumentalities, which are generally not supported by the full faith and credit of the United States, may be more exposed to credit risk.

Call and Redemption Risk. A bond s issuer may call a bond for redemption before it matures. If this happens to a bond the Fund holds, the Fund may lose income and may have to invest the proceeds in bonds with lower yields.

Income Risk. The income shareholders receive from the Fund is based primarily on the interest it earns from its investments as well as the gains the Fund receives from writing options and selling portfolio securities, each of which can vary widely over the short and long term. If prevailing market interest rates decline, interest rates on debt securities held by the Fund, and shareholders income from the Fund, would likely decline as well.

Net Asset Value; Interest Rate Sensitivity; Credit Quality; Other Market Conditions. Generally, when interest rates go up, the value of fixed income securities, such as U.S. Government securities that pay fixed interest rates, goes down. Because market interest rates are currently near their lowest levels in many years, there is a greater risk that interest rates may increase in the future and cause the value of certain securities held in the Fund s portfolio to decline. In addition, when market interest rates rise, not only may the Fund s investment portfolio decline in value, but the cost of leverage, if any, may increase. See Risk Factors and Special Considerations Leverage Risk. Therefore, the net asset value of the Fund will change as interest rates fluctuate to the extent that the Fund invests in fixed income securities. During periods of rising interest rates, the average life of certain types of securities may be extended because of slower than expected principal payments. This may lock in a below market interest rate, increase the duration and reduce the value of the security. Volatility in the capital markets and other adverse market conditions may result in a decrease in the value of the securities held by the Fund. Any decrease in the market value of the securities held by the Fund will result in a decrease in the Fund s net asset value and potentially the market price of the Fund s common stock.

Other Portfolio Strategies. In addition to writing (selling) call options, the Fund may engage in various other portfolio strategies to seek to increase the return of the Fund and to seek to hedge its portfolio against adverse effects from movements in interest rates and in the securities markets. These additional strategies include the use of derivative instruments, such as purchased call options, purchased or written put options, indexed securities, inverse securities, options, futures, options on futures, interest rate transactions, credit default swaps, interest rate swaps, options on swaps, total return swaps, short sales and foreign exchange transactions. Such strategies subject the Fund to the risk that, if the Investment Adviser incorrectly forecasts market values, interest rates or other applicable factors, the Fund s performance could suffer. Certain of these strategies such as inverse securities, credit default swaps, interest rate swaps, total return swaps and short sales may provide investment leverage to the Fund s portfolio and result in many of the same risks of leverage to the holders of the Fund s common stock as discussed below under Other Investment Policies Leverage. The Fund is not required to use derivatives or other portfolio strategies to increase return or to hedge its portfolio and may choose not to do so. No assurance can be given that the Fund s portfolio strategies will be effective. Some of the derivative strategies that the Fund may use to increase its return are riskier than its hedging transactions and have speculative characteristics. Such strategies do not attempt to limit the Fund s risk of loss.

General Risks Related to Derivatives. As noted above, derivatives are financial contracts or instruments whose value depends on, or is derived from, the value of an underlying asset, reference rate or index (or relationship between two indices). The Fund also may have exposure to derivatives through investment in credit

linked notes, credit linked trust certificates and other securities issued by special purpose or structured vehicles. The Fund may use derivatives as a substitute for taking a position in an underlying security or other asset, or as part of a strategy designed to reduce exposure to other risks, such as interest rate risk. The Fund s use of derivative instruments involves risks different from, and possibly greater than, the risks associated with investing directly in securities and other traditional investments. Derivatives are subject to a number of risks, such as liquidity risk, interest rate risk, credit risk, counterparty risk, leverage risk, the risk of ambiguous documentation and management risk. Counterparty risk is the risk that the financial status of the derivative counterparty may affect the ability of the Fund to receive payments under the applicable derivative instrument. They also involve the risk of mispricing or improper valuation and correlation risk (*i.e.,* the risk that changes in the value of the derivative may not correlate perfectly with the underlying asset, rate or index). If the Fund invests in a derivative instrument it could lose more than the principal amount invested. The use of derivatives also may increase the amount of taxes payable by stockholders. Also, suitable derivative transactions may not be available in all circumstances and no assurance can be given that the Fund will engage in these transactions to reduce exposure to other risks when that would be beneficial.

Foreign Securities. The Fund may invest up to 20% of its net assets in debt securities of issuers domiciled outside the United States. The Fund s investments in such issuers involve certain risks that are not involved in domestic investments, including fluctuation in foreign interest rates, future foreign political and economic developments and the possible imposition of exchange controls or other governmental laws or regulations.

Annual Repurchases of Fund Shares. The Fund has an interval fund structure, pursuant to which the Fund will conduct, subject to applicable Maryland law, annual repurchase offers for between 5% and 25% of the Fund s outstanding shares. These required annual repurchases are likely to decrease the overall size of the Fund, which could over time: (i) harm the Fund s investment performance by limiting the extent to which the Fund may invest in illiquid securities; (ii) increase the Fund s expense ratio as the Fund s assets decrease; (iii) threaten the Fund s continued listing of its shares of common stock on the New York Stock Exchange, and, consequently, the liquidity of its shares; and (iv) jeopardize the Fund s viability and continued existence. Moreover, there are additional risks associated with the Fund s annual repurchase offers, including the risk that: (i) because a repurchase offer will be for 5% to 25% of the Fund s outstanding shares, if the repurchase offer is oversubscribed, stockholders may be unable to liquidate all or a given percentage of their investment at net asset value during the repurchase offer; (ii) due to the potential for the Fund to purchase shares on a pro rata basis if the repurchase offer is over-subscribed, some investors may tender more shares than they wish to have repurchased in order to ensure the repurchase of a specific number of shares; (iii) the repurchase offer may not eliminate any discount at which the Fund s shares trade; and (iv) because the Fund expects, in certain circumstances, to liquidate portfolio securities in order to fund repurchase offers, the need to sell such securities may in turn affect the market for such securities and accordingly diminish the value of the Fund s investments. Furthermore, to the extent the Fund borrows to finance the making of repurchases, interest on such borrowings reduce the Fund s returns. See Annual Repurchases of Fund Shares for more information regarding the interval fund structure.

Set forth below are certain other risks associated with investing in the Fund s common stock.

Ratings Categories. The Fund may invest up to 20% of its net assets in non-U.S. Government debt securities that are rated investment grade or, if unrated, are considered by the Investment Adviser to be of comparable quality. Obligations rated in the lowest investment grade category may have certain speculative characteristics. For example, their prices may be more volatile, economic downturns and financial setbacks may affect their prices more negatively, and their trading market may be more limited than higher rated securities.

Borrowing and Leverage Risk. The Fund may borrow for temporary or emergency purposes, including for the payment of dividends, for share repurchases or for the clearance of transactions. Borrowing may exaggerate changes in the net asset value of Fund shares and in the return on the Fund s portfolio. Borrowing will cost the Fund interest expense and other fees. The costs of borrowing may reduce the Fund s return. Certain derivative securities that the Fund may buy or other techniques that the Fund may use may create leverage, including, but not limited to, when issued securities, forward commitments and futures contracts and options.

Inflation/Deflation Risk. Inflation risk is the risk that the value of assets or income from the Fund s investment will be worth less in the future as inflation decreases the value of money. As inflation increases, the real, or inflation adjusted, value of the Fund s common stock and distributions can decline and the interest payments on Fund borrowings, if any, may increase or the dividend payments on the Fund s preferred stock, if any, may increase. Deflation risk is the risk that prices throughout the economy decline over time the opposite of inflation. Deflation may have an adverse effect on the creditworthiness of issuers and may make issuer default more likely, which may result in a decline in the value of the Fund s portfolio.

Securities Lending. The Fund may lend securities with a value up to $33^1/3$ % of its total assets to financial institutions that provide cash or securities issued or guaranteed by the U.S. Government as collateral. Securities lending involves the risk that the borrower may fail to return the securities in a timely manner or at all. As a result, the Fund may lose money and there may be a delay in recovering the loaned securities. The Fund could also lose money if it does not recover the securities and/or the value of the collateral falls, including the value of investments made with cash collateral. These events could trigger adverse tax consequences to the Fund.

Futures Transactions. Futures are types of derivatives. The Fund may engage in futures transactions to reduce its exposure to interest rate movements or to enhance its return. If the Fund incorrectly forecasts market values, interest rates or other factors, the Fund s performance could suffer. The Fund also may suffer a loss if the other party to the transaction fails to meet its obligations. The Fund is not required to enter into futures transactions for hedging purposes or to increase its return and may choose not to do so.

Swaps. Swap agreements are types of derivatives. In order to seek to hedge the value of the Fund s portfolio, to hedge against increases in the Fund s costs associated with the interest payments on its outstanding borrowings or the dividend payments on its outstanding preferred stock, if any, or to seek to increase the Fund s return, the Fund may enter into interest rate, credit default or total return swap transactions. In interest rate swap transactions, there is a risk that yields will move in the direction opposite to the direction anticipated by the Fund, which would cause the Fund to make payments to its counterparty in the transaction that could adversely affect Fund performance. In addition to the risks applicable to swaps generally, credit default swap transactions involve special risks because they may be difficult to value, are susceptible to liquidity and credit risk, and generally pay a return to the party that has paid the premium only in the event of an actual default by the issuer of the underlying obligation (as opposed to a credit downgrade or other indication of financial difficulty). Total return swap transactions involve the risks that the counterparty will default on its payment obligation to the Fund in the transaction and that the Fund will not be able to meet its obligation to the counterparty in the transaction. The Fund is not required to enter into interest rate, credit default or total return swap transactions for hedging purposes or to increase its return and may choose not to do so. The Fund may also purchase or sell options on swap transactions.

Short Sales. The Fund may make short sales of securities. A short sale is a transaction in which the Fund sells a security it does not own in anticipation that the market price of that security will decline. When the Fund makes a short sale, it must borrow the security sold short and deliver collateral to the broker dealer through

which it made the short sale to cover its obligation to deliver the borrowed security upon conclusion of the sale. The Fund s obligation to replace the borrowed security will be secured by collateral deposited with the broker dealer, usually cash, U.S. government securities or other liquid securities similar to those borrowed. The Fund will also be required to segregate similar collateral with its custodian. If the price of the security sold short increases between the time of the short sale and the time the Fund replaces the borrowed security, the Fund will incur a loss. The Fund also may make a short sale (against the box) by selling a security that the Fund owns or has the right to acquire without the payment of further consideration. The Fund s potential for loss is greater if it does not own the security that it is short selling.

Leverage Risk. Although the Fund has no present intention to use leverage, it may in the future leverage its portfolio through borrowings, the issuance of debt securities, the issuance of preferred stock or a combination thereof. The Fund may borrow money and issue debt securities in amounts up to $33^{1}/3$ %, and may issue shares of preferred stock in amounts up to 50%, of the value of its total assets to finance additional investments. No assurance can be given that the Fund will not leverage its portfolio.

The use of leverage creates certain risks for common stockholders, including the greater likelihood of higher volatility of the Fund s dividend yield, total return, net asset value and the market price of the common stock. An additional risk of leverage is that the cost of the leverage plus applicable Fund expenses may exceed the return on the securities acquired with the proceeds of the leverage, thereby diminishing rather than enhancing the return to the Fund s common stockholders. During times of rising interest rates, the market value of the Fund s portfolio investments may decline, while at the same time the Fund s cost of leverage may increase. These risks would generally make the Fund s return to common stockholders more volatile if it were to use leverage. So long as the Fund uses leverage, it may be required to sell investments in order to make interest or dividend payments on borrowings or preferred stock used for leverage when it may be disadvantageous to do so. Finally, if the Fund uses leverage and the asset coverage for the Fund s borrowings or preferred stock declines to less than 300% or 200% of the Fund s total assets, respectively, or below asset coverage requirements established by a rating agency that rated any preferred stock or debt security issued by the Fund (as a result of market fluctuations or otherwise), the Fund may be required to sell a portion of its investments to repay the borrowings or redeem some or all of the preferred stock or debt securities when it may be disadvantageous to do so. No assurance can be given that any leverage strategy used by the Fund will be successful.

Rating Agencies. In the event the Fund issues preferred stock, the Fund may be subject to guidelines of one or more rating agencies that may issue ratings for such preferred stock. These guidelines may impose asset coverage or portfolio composition requirements that are more stringent than those imposed by the 1940 Act and may prohibit or limit the use by the Fund of certain portfolio management techniques or investments. The Fund does not expect these guidelines to prevent the Investment Adviser from managing the Fund s portfolio in accordance with the Fund s investment objectives and policies.

Tax Risk. Certain transactions entered into by the Fund are subject to special tax rules that may, among other things, (i) affect the character of gains and losses realized, (ii) disallow, suspend or otherwise limit the allowance of certain losses or deductions and (iii) accelerate the recognition of income without a corresponding receipt of cash (with which to make the necessary distributions to satisfy distribution requirements applicable to regulated investment companies). Operation of these rules could, therefore, affect the character, amount and timing of distributions to stockholders. Special tax rules also will require the Fund to mark to market certain types of positions in its portfolio, including some of its call options (*i.e.,* treat them as sold on the last day of the taxable year), and may result in the recognition of income without a corresponding receipt of cash. The Fund intends to monitor its transactions, to make appropriate tax elections and to make appropriate entries in its books

and records to lessen the effect of these tax rules and avoid any possible disqualification for the favorable tax treatment afforded regulated investment companies. In addition, there is a possibility that the Fund may make total distributions during a calendar or fiscal year in an amount that exceeds the Fund s net investment income and net realized capital gains for the relevant fiscal year. In such situations, the amount by which the Fund s total distributions exceed net investment income and net realized capital gains would generally be treated as a tax-free return of capital up to the amount of a stockholder s tax basis in his or her shares, with any amounts exceeding such basis treated as gain from the sale of shares.

Under current law, certain dividend income is eligible for taxation at a lower rate that is also applicable to long term capital gains in the hands of individual stockholders. Certain tax rules may limit the Fund s ability to designate dividends as long term capital gains eligible for taxation at reduced rates. Short term capital gains and interest income on debt securities are not eligible for this reduced tax rate. In addition, gains from writing call options generally will not be eligible for taxation at a reduced rate.

The Fund s investments and the tax treatment of Fund distributions may be affected by future changes in tax laws and regulations, including changes as a result of the sunset provisions that currently apply to the reduced federal income tax rate for long term capital gains. The impact of such legislation on the Fund and its stockholders cannot be predicted.

Liquidity of Investments. Certain securities and derivative instruments in which the Fund invests may lack an established secondary trading market or are otherwise considered illiquid. Liquidity of a security or instrument relates to the ability to easily dispose of the security or instrument and the price to be obtained and does not generally relate to the credit risk or likelihood of receipt of cash at maturity. Illiquid securities or investments may trade at a discount from comparable, more liquid investments.

Indexed and Inverse Floating Rate Securities. The Fund may invest in securities whose potential returns are directly related to changes in an underlying index or interest rate, known as indexed securities. The return on indexed securities will rise when the underlying index or interest rate rises and fall when the index or interest rate falls. The Fund may also invest in securities whose return is inversely related to changes in an interest rate (inverse floaters). In general, income on inverse floaters will decrease when interest rates increase and increase when interest rates decrease. Investments in inverse floaters may subject the Fund to the risks of reduced or eliminated interest payments and losses of principal. In addition, certain indexed securities and inverse floaters may increase or decrease in value at a greater rate than the underlying interest rate, which effectively leverages the Fund s investment. Indexed securities and inverse floaters are derivative securities and can be considered speculative. Indexed and inverse securities involve credit risk and certain indexed and inverse securities may involve currency risk, leverage risk and liquidity risk.

Repurchase Agreements. The Fund may enter into certain types of repurchase agreements. Under a repurchase agreement, the seller agrees to repurchase a security at a mutually agreed upon time and price. If the other party to a repurchase agreement defaults on its obligation, the Fund may suffer delays and incur costs or even lose money in exercising its rights under the agreement.

When Issued Securities, Delayed Delivery Securities and Forward Commitments. When issued and delayed delivery securities and forward commitments involve the risk that the security the Fund buys will lose value prior to its delivery. There also is the risk that the security will not be issued or that the other party will not meet its obligation. If this occurs, the Fund both loses the investment opportunity for the assets it has set aside to pay for the security and any gain in the security s price.

Restricted Securities. Restricted securities are securities that cannot be offered for public resale unless registered under applicable securities laws. The restric