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FILER

KEYSTONE TAX FREE FUND

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PROSPECTUS	APRIL 28, 1995

KEYSTONE TAX FREE FUND
200 BERKELEY STREET, BOSTON, MASSACHUSETTS 02116-5034
CALL TOLL FREE 1-800-343-2898

Keystone Tax Free Fund (the "Fund") is a mutual fund that seeks the highest possible current income, exempt from federal income taxes, while preserving capital. The Fund invests primarily in municipal bonds. The Fund's net asset value per share will fluctuate in response to changes in the market value of its portfolio securities.

Except as noted below, the Fund generally offers its shares by direct investment only to those shareholders who already beneficially own shares of the Fund. The Fund also offers its shares through exchanges to shareholders of certain other funds in the Keystone Investments Family of Funds. Beginning May 1, 1995, the Fund will be reopen to new investors. It is presently intended that the Fund remain open until July 31, 1995 or until the Fund attains $50,000,000 in aggregate sales, whichever occurs first (the "Special Offering Period").

Your purchase payment is fully invested. There is no sales charge when you buy the Fund's shares. The Fund may impose a deferred sales charge, which declines from 4% to 1%, if you redeem your shares within four years of purchase.

The Fund has adopted a Distribution Plan (the "Distribution Plan") pursuant to Rule 12b-1 under the Investment Company Act of 1940 (the "1940 Act") under which it bears some of the costs of selling its shares to the public.

This prospectus sets forth concisely the information about the Fund that you should know before investing. Please read it and retain it for future reference.

Additional information about the Fund is contained in a statement of additional information dated April 28, 1995, which has been filed with the Securities and Exchange Commission and is incorporated by reference into this prospectus. For a free copy, or for other information about the Fund, write to the address or call the telephone number listed above.

SHARES OF THE FUND ARE NOT DEPOSITS OR OBLIGATIONS OF, OR GUARANTEED OR ENDORSED BY, ANY BANK, AND SHARES ARE NOT FEDERALLY INSURED BY THE FEDERAL DEPOSIT INSURANCE CORPORATION, THE FEDERAL RESERVE BOARD, OR ANY OTHER AGENCY.

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THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION NOR HAS THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

FEE TABLE

KEYSTONE TAX FREE FUND

The purpose of the fee table is to assist investors in understanding the costs and expenses that an investor in the Fund will bear directly or indirectly. For more complete descriptions of the various costs and expenses, see the following sections of this prospectus: "Fund Management and Expenses"; "How to Buy Shares"; "Distribution Plan"; and "Shareholder Services."

SHAREHOLDER TRANSACTION EXPENSES

Contingent Deferred Sales Charge\1/ .... (as a percentage of the lesser of total cost or net asset value of shares redeemed)	4.00%
Exchange Fee\2/ .... (per exchange)	$10.00

ANNUAL FUND OPERATING EXPENSES\3/
(as a percentage of average net assets)

Management Fees	0.43%
12b-1 Fees\4/	0.61%
Other Expenses	0.15%

Total Fund Operating Expenses	1.19%
	=====

EXAMPLE\5/	1 Year	3 Years	5 Years	10 Years
You would pay the following expenses on a $1,000 investment, assuming (1) 5% annual return and (2) redemption at the end of each period:	$52.00	$58.00	$65.00	$144.00
You would pay the following expenses on the same investment, assuming no redemption:	$12.00	$38.00	$65.00	$144.00

AMOUNTS SHOWN IN THE EXAMPLE SHOULD NOT BE CONSIDERED A REPRESENTATION OF PAST OR FUTURE EXPENSES; ACTUAL EXPENSES MAY BE GREATER OR LESS THAN THOSE SHOWN.
- ---------

(1) The deferred sales charge declines from 4% to 1% of amounts redeemed within four calendar years after purchase. No deferred sales charge is imposed thereafter.
(2) There is no exchange fee for exchange orders received by the Fund from an individual shareholder over the Keystone Automated Response Line ("KARL"). (For a description of KARL, see "Shareholder Services.")
(3) To reflect current fees, expense ratios are estimated for the Fund's fiscal year ending December 31, 1995. The estimated expense ratios reflect certain actions taken by the Fund's Board of Trustees, in connection with the reopening of the Fund on May 1, 1995, with respect to the maximum annual expenditures permitted under the Fund's Distribution Plan. See "Distribution Plan."
(4) Long-term shareholders may pay more than the economic equivalent of the maximum front end sales charge permitted by rules adopted by the National Association of Securities Dealers, Inc. ("NASD"). See "Distribution Plan."
(5) The Securities and Exchange Commission requires use of a 5% annual return figure for purposes of this example. Actual return for the Fund may be greater or less than 5%.

FINANCIAL HIGHLIGHTS

KEYSTONE TAX FREE FUND

(For a share outstanding throughout the year)

The following table contains important financial information relating to the Fund and has been audited by KPMG Peat Marwick LLP, the Fund's independent auditors. The table appears in the Fund's Annual Report and should be read in conjunction with the Fund's financial statements and related notes, which also appear, together with the independent auditors' report, in the Fund's Annual Report. The Fund's financial statements, related notes, and independent auditors' report are included in the statement of additional information. Additional information about the Fund's performance is contained in its Annual Report, which will be made available upon request and without charge.

<TABLE>
<CAPTION>

	YEAR ENDED DECEMBER 31,									
	1994	1993	1992	1991	1990(d)	1989	1988	1987	1986	1985
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
NET ASSET VALUE: BEGINNING OF YEAR	$ 8.12	$ 8.04	$ 8.07	$ 7.90	$ 8.06	$ 8.18	$ 8.09	$ 8.85	$ 8.31	$ 7.57
Income from investment operations										
Net investment income	0.37	0.39	0.46	0.46	0.52	0.57	0.55	0.56	0.68	0.70
Net gains (losses) on investments	(0.96)	0.48	0.12	0.36	(0.01)	0.15	0.30	(0.58)	0.88	0.81
Net commissions paid on fund share sales (b)	-0-	-0-	-0-	-0-	-0-	-0-	-0-	-0-	(0.08)	(0.07)
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Total from investment operations	(0.59)	0.87	0.58	0.82	0.51	0.72	0.85	(0.02)	1.48	1.44
Less distributions from										
Investment income -- net(a)	(0.37)	(0.39)	(0.46)	(0.46)	(0.52)	(0.60)	(0.63)	(0.64)	(0.68)	(0.70)
In excess of investment income -- net	(0.06)	(0.06)	(0.04)	(0.07)	(0.03)	-0-	-0-	-0-	-0-	-0-
Realized capital gains -- net	-0-	(0.33)	(0.11)	(0.12)	(0.12)	(0.24)	(0.13)	(0.10)	(0.26)	-0-
In excess of realized capital gains -- net	-0-	(0.01)	-0-	-0-	-0-	-0-	-0-	-0-	-0-	-0-
Total distributions	(0.43)	(0.79)	(0.61)	(0.65)	(0.67)	(0.84)	(0.76)	(0.74)	(0.94)	0.70)
NET ASSET VALUE: END OF YEAR	$ 7.10	$ 8.12	$ 8.04	$ 8.07	$ 7.90	$ 8.06	$ 8.18	$ 8.09	$ 8.85	$ 8.31
TOTAL RETURN(C)	(7.34%)	11.15%	7.55%	10.80%	6.66%	9.11%	10.89%	(0.14%)	18.26%	19.96%
RATIOS/SUPPLEMENTAL DATA										
Ratios to average net assets:										
Operating and management expenses	1.55%	1.66%	1.38%	1.75%	1.18%	1.23%	1.79%	1.70%	0.83%	0.92%
Investment income - net	4.92%	4.72%	5.71%	5.78%	6.54%	6.94%	6.74%	6.80%	7.79%	8.65%
Portfolio turnover rate	84%	76%	78%	77%	64%	69%	61%	43%	44%	55%
Net assets, end of year (thousands)	$1,197,727	1,548,503	$1,453,199	$1,146,185	$1,060,826	$901,912	$903,132	$894,768	$1,025,084	863,720

</TABLE>

NOTES TO FINANCIAL HIGHLIGHTS

(a) Effective January 1, 1993 the Fund adopted Statement of Position 93-2: "Determination, Disclosure, and Financial Statement Presentation of Income, Capital Gain and Return of Capital Distributions by Investment Companies. "As a result, distribution amounts exceeding book basis investment income--net (or tax basis net income on a temporary basis) are presented as "Distributions in excess of investment income--net." Similarly, capital gain distributions in excess of book basis gains (or tax basis capital gains on a temporary basis) are presented as "Distributions in excess of realized capital gains." For the fiscal years ended December 31, 1992, 1991 and 1990, distributions in excess of book basis net income were presented as "distribution from paid-in capital."

(b) Prior to June 30, 1987, net commissions paid on new sales of shares under the Fund's Rule 12b-1 Distribution Plan had been treated for both financial statement and tax purposes as capital charges. On June 11, 1987, the Securities and Exchange Commission adopted a rule that required for financial statements for the periods ended on or after June 30, 1987, that net commissions paid under Rule 12b-1 be treated as operating expenses rather than capital charges. Accordingly, beginning with the year ended December 31, 1987, the Fund's financial statements reflect 12b-1 Distribution Plan expenses (i.e., shareholder service fees plus commissions paid net of deferred sales charges received by the Fund) as a component of net investment income.

(c) Excluding contingent deferred sales charges.

(d) Calculation based on average shares outstanding.

FUND DESCRIPTION

The Fund is an open-end, diversified, management investment company, commonly known as a mutual fund. The Fund has been operating continuously since April 12, 1977 when it was created under Massachusetts law as a Massachusetts business trust. The Fund is one of twenty funds managed by Keystone Management, Inc. ("Keystone Management"), the Fund's investment manager, and is one of twenty-nine funds managed or advised by Keystone Investment Management Company (formerly Keystone Custodian Funds, Inc.) ("Keystone"), the Fund's investment adviser. Keystone and Keystone Management are, from time to time, also collectively referred to as "Keystone."

FUND OBJECTIVE AND POLICIES

The Fund's investment objective is to provide shareholders with the highest possible current income, exempt from federal income taxes, while preserving capital.

The Fund invests substantially all and, under ordinary circumstances, at least 80% of its assets in federally tax-exempt obligations, including municipal bonds and notes and tax-exempt commercial paper (municipal bonds), which are obligations issued by or on behalf of states, territories and possessions of the United States ("U.S."), the District of Columbia and their political subdivisions, agencies and instrumentalities, the interest from which is, in the opinion of counsel to the issuers of such bonds, exempt from federal income taxes, including the alternative minimum tax.

Municipal bonds include debt obligations issued by or on behalf of a political subdivision of the U.S. or any agency or instrumentality thereof to obtain funds for various public purposes. In addition, municipal bonds include certain types of industrial revenue bonds issued by or on behalf of public authorities to finance privately operated facilities.

General obligation bonds involve the credit of an issuer possessing taxing power and are payable from the issuer's general unrestricted revenues. Their payment may be dependent upon an appropriation by the issuer's legislative body and may be subject to quantitative limitations on the issuer's taxing power. Limited obligation or revenue bonds are payable only from the revenues of a particular facility or class of facilities or, in some cases, from the proceeds of a special excise or other specific revenue source, such as the user of the facility.

Since the Fund considers preservation of capital as well as the level of tax exempt income, the Fund may realize less income than a fund willing to expose shareholders' capital to greater risk.

The Fund invests in municipal bonds only if, at the date of investment, they are rated within the four highest grades by Standard & Poor's Corporation ("S&P") (AAA, AA, A and BBB), by Moody's Investors Service, Inc. ("Moody's") (Aaa, Aa, A and Baa) or by Fitch Investors Service, Inc. -- Municipal Division ("Fitch") (AAA, AA, A and BBB) or, if not rated, are of comparable quality to obligations so rated as determined by Keystone.

Bonds rated Baa by Moody's are considered to be medium grade obligations, i.e., they are neither highly protected nor poorly secured. Interest payments and principal security appear adequate for the present, but certain protective elements may be lacking or may be characteristically unreliable over any great length of time. Such bonds lack outstanding investment characteristics and have speculative characteristics as well.

Debt rated BBB by S&P is regarded as having an adequate capacity to pay interest and repay principal. While it normally exhibits adequate protection parameters, adverse economic conditions or changing circumstances are generally more likely to lead to a weakened capacity to pay interest and repay principal for debt in this category than in high rated categories.

Bonds rated BBB by Fitch are considered to be investment grade and of satisfactory credit quality. The obligator's ability to pay interest and repay principal is considered to be adequate. Adverse changes in economic conditions and circumstances, however, are more likely to have adverse impact on these bonds, and therefore impair timely payment. The likelihood that the ratings of these bonds will fall below investment grade is higher than for bonds with higher ratings.

Keystone expects that under normal circumstances at least 65% of the Fund's total assets invested in municipal bonds will be within the three highest ratings of such services or, if not rated, will be of comparable quality.

The Tax Reform Act of 1986 made significant changes in the federal tax status of certain obligations that previously were fully federally tax-exempt. As a result, three categories of such obligations issued after August 7, 1986 now exist: (1) "public purpose" bonds, the income from which remains fully exempt from federal income taxes; (2) qualified "private activity" industrial development bonds, the income from which, while exempt from federal income taxes under Section 103 of the Internal Revenue Code ("the Code"), is includable in the calculation of the federal alternative minimum tax; and (3) "private activity" (private purpose) bonds, the income from which is not exempt from federal income taxes. Investments in qualified "private activity" industrial development bonds will be limited by the Fund's policy of investing no more than 20% of its total assets in securities that pay interest that is not exempt from federal taxation. The Fund currently will not invest in "private activity" (private purpose) bonds.

The Fund also may invest in securities that pay interest that is not exempt from federal income taxes, such as corporate and bank obligations, obligations issued or guaranteed by the U.S. government or by any of its agencies or instrumentalities, commercial paper and repurchase agreements. Such securities must be rated at least BBB by S&P or Baa by Moody's or, if not rated, must be determined by Keystone to be of comparable quality. However, except for temporary defensive purposes, the Fund will not invest more than 20% of its total assets in such securities.

The Fund also may enter into reverse repurchase agreements and firm commitment agreements for securities and currencies. The Fund may enter into options transactions and may write covered call and put options, purchase call and put options, including purchasing call and put options to close out existing positions, and purchase call options to fix the interest rates of obligations held by it. The Fund may also employ new investment techniques involving such options. In addition, the Fund may enter into currency and other financial futures contracts and related options transactions for hedging purposes and not for speculation and employ new investment techniques with respect to such futures contracts and related options. In addition, the Fund may also invest in obligations denominated in foreign currencies that are exempt from federal income tax.

In addition to the options and futures contracts mentioned above, only if it is consistent with its investment objective, the Fund may also invest in certain other types of "derivative instruments," including structured securities.

In addition, the Fund may, notwithstanding any other investment policy or restriction, invest all of its assets in the securities of a single open-end management investment company with substantially the same fundamental investment objectives, policies and restrictions as the Fund. The Fund does not currently intend to implement this policy and would do so only if the Trustees were to determine such action to be in the best interest of the Fund and its shareholders. In the event of such implementation, the Fund will comply with such requirements as to written notice to shareholders as are then in effect.

For further information about the types of investments and investment techniques available to the Fund, including the associated risks, see the section of this prospectus entitled "Additional Investment Information" and the statement of additional information.

FUNDAMENTAL NATURE OF INVESTMENT OBJECTIVE

The investment objective of the Fund set forth above is fundamental and may not be changed without the vote of a majority of the Fund's outstanding shares (which means the lesser of (1) 67% of the shares represented at a meeting at which more than 50% of the outstanding shares are represented or (2) more than 50% of the outstanding shares). Of course, there can be no assurance that the Fund will achieve its investment objective since there is uncertainty in every investment.

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INVESTMENT RESTRICTIONS

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The Fund has adopted the fundamental restrictions summarized below, which may not be changed without the approval of a majority of the Fund's outstanding shares. These restrictions and certain other fundamental and non-fundamental restrictions are set forth in detail in the statement of additional information.

Generally, the Fund may not do the following: (1) invest more than 5% of its total assets in the securities of any one issuer; (2) borrow money, except that the Fund may borrow money from banks for emergency or extraordinary purposes in aggregate amounts up to one-third (normally less than 5%) of its net assets and enter into reverse repurchase agreements; (3) pledge more than 15% of its total assets to secure borrowings; and (4) invest more than 25% of its total assets in securities of issuers in the same industry;

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RISK FACTORS

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GENERAL

The risk inherent in investing in the Fund is the risk common to investing in any security, i.e., the net asset value will fluctuate in response to changes in economic conditions, interest rates and the market's perception of the underlying portfolio securities of the Fund.

The Fund is not intended to constitute a balanced investment program and is not designed for investors seeking capital appreciation or maximum tax-exempt income irrespective of fluctuations in principal or marketability. Shares of the Fund would not be suitable for tax-exempt institutions and may not be suitable for certain retirement plans that are unable to benefit from the Fund's tax-exempt dividends. In addition, the Fund may not be an appropriate investment for entities that are "substantial users" of facilities financed by industrial development bonds or related persons thereof.

MUNICIPAL OBLIGATIONS

The ability of the Fund to achieve its investment objective is dependent upon the continuing ability of issuers of municipal bonds to meet their obligations to pay interest and principal when due. Obligations of issuers of municipal bonds, including municipal bonds issued by them, are subject to the provisions of bankruptcy, insolvency and other laws affecting the rights and remedies of creditors, such as the federal Bankruptcy Act and laws, if any, that may be enacted by Congress or state legislatures extending the time for payment of principal or interest, or both, or imposing other constraints upon enforcement of such obligations. There is also the possibility that as a result of litigation or other conditions, the power or ability of any one or more issuers to pay, when due, principal and interest on its or their municipal bonds may be materially affected. In addition, the market for municipal bonds is often thin and can be temporarily affected by large purchases and sales, including those by the Fund.

From time to time, proposals have been introduced before Congress for the purpose of restricting or eliminating the federal income tax exemption for interest on municipal bonds, and similar proposals may be introduced in the future. If such a proposal were enacted, the availability of municipal bonds for investment by the Fund and the value of the Fund's portfolio could be materially affected, in which event, the Fund would re-evaluate its investment objective and policies and consider changes in the structure of the Fund or dissolution.

OTHER CONSIDERATIONS

Investment in some securities may involve special considerations. For example, the Fund may invest in master demand notes, a type of commercial paper that is redeemable on demand, but for which there is no secondary market. Furthermore, the Fund may enter into repurchase agreements with domestic banks and broker-dealers. The payment of interest accrued by the Fund under its repurchase agreements is dependent on the ability of the seller to perform its obligations to the Fund. If the seller of a repurchase agreement refused to repurchase the securities underlying the agreement, the Fund would suffer a loss if the proceeds from the sale of the underlying securities were less than the agreed upon repurchase price, and the loss would be increased by any cost of selling the securities. If the defaulting seller filed for bankruptcy or became insolvent, the sale of the securities might be delayed by pending court action. In such a case, it is not clear that the Fund would have the right, against other claimants, to keep the securities.

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PRICING SHARES

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The net asset value of a Fund share is computed each day on which the New York Stock Exchange (the "Exchange") is open as of the close of trading on the Exchange (currently 4:00 p.m. eastern time for the purpose of pricing Fund shares) except on days when changes in the value of the Fund's securities do not affect the current net asset value of its shares. The Exchange currently is closed on weekends, New Year's Day, Presidents' Day, Good Friday, Memorial Day, Independence Day, Labor Day, Thanksgiving Day and Christmas Day. The net asset value per share is arrived at by determining the value of all of the Fund's assets, subtracting all liabilities and dividing the result by the number of shares outstanding.

The Fund values municipal bonds on the basis of valuations provided by a pricing service, approved by the Fund's Board of Trustees, which uses information with respect to transactions in bonds, quotations from bond dealers, market transactions in comparable securities and various relationships between securities in determining value. The Fund values short-term instruments with maturities of sixty days or less at amortized cost (original purchase cost as adjusted for amortization of premium or accretion of discount), which, when combined with accrued interest, approximates market. Short-term instruments maturing in more than sixty days for which market quotations are readily available are valued at current market value. Short-term instruments maturing in more than sixty days when purchased that are held on the sixtieth day prior to maturity are valued at amortized cost (market value on the sixtieth day adjusted for amortization of premium or accretion of discount), which, when combined with accrued interest, approximates market and which in any case reflects fair value as determined by the Fund's Board of Trustees. All other investments are valued at market value or, where market quotations are not readily available, at fair value as determined in good faith using methods prescribed by the Fund's Board of Trustees.

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DIVIDENDS AND TAXES

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The Fund has qualified and intends to qualify in the future as a regulated investment company under the Code. The Fund qualifies if, among other things, it distributes to its shareholders at least 90% of its net investment income for its fiscal year. The Fund also intends to make timely distributions, if necessary, sufficient in amount to avoid the nondeductible 4% excise tax imposed on a regulated investment company to the extent that it fails to distribute, with respect to each calendar year, at least 98% of its ordinary income for such calendar year and 98% of its net capital gains for the one-year period ending on October 31 of such calendar year. Any taxable distribution would be (1) declared in October, November, or December to shareholders of record in such a month, (2) paid by the following January 31, and (3) includable in the taxable income of shareholders for the year in which such distributions were declared. If the Fund qualifies and if it distributes substantially all of its net investment income and net capital gains, if any, to shareholders, it will be relieved of any federal income tax liability.

As of April 1, 1995, in compliance with a recent ruling issued by the Internal Revenue Service ("IRS"), the Fund treats its 12b-1 fees for tax purposes as operating expenses, rather than capital charges.

The Fund intends to declare dividends from net investment income daily and distribute to its shareholders such dividends monthly and to declare and distribute all net realized long-term capital gains annually. All dividends and distributions will be payable in shares or, at the option of the shareholder, in cash. All shareholders may receive dividends in shares without being subject to a deferred sales charge when such shares are redeemed. Shareholders who have not opted prior to the record date for any distribution to receive cash will have the number of such shares determined on the basis of the Fund's net asset value per share computed at the end of the day on the record date after adjustment for the distribution. Net asset value is used in computing the number of shares in both capital gains and income distribution reinvestments. There is a possibility that shareholders may lose the tax-exempt status on accrued income on municipal bonds if shares of the Fund are redeemed before a dividend has been declared. Account statements and/or checks as appropriate will be mailed to shareholders within seven days after the Fund pays the distribution. Unless the Fund receives instructions to the contrary from a shareholder before the record date, it will assume that the shareholder wishes to receive that distribution and future capital gains and income distributions in shares. Instructions continue in effect until changed in writing.

Under normal circumstances, the Fund expects that substantially all of its dividends will be "exempt interest dividends," which will be treated by its shareholders as excludable from federal gross income. In order to pay exempt interest dividends, at the close of each quarter at least 50% of the value of the Fund's assets must consist of federally tax-exempt obligations. An exempt interest dividend is any dividend or part thereof (other than a capital gain dividend) paid by the Fund with respect to its net federally excludable municipal bond interest and designated as an exempt interest dividend in a written notice mailed to shareholders not later than sixty days after the close of its taxable year. The percentage of the total dividends paid by the Fund with respect to any taxable year that qualifies as exempt interest dividends will be the same for all shareholders receiving dividends with respect to such year. If a shareholder receives an exempt interest dividend with respect to any share and such share is held for six months or less, any loss on the sale or exchange of such share will be disallowed to the extent of the exempt interest dividend amount.

Any shareholder who may be a "substantial user" of a facility financed with an issue of tax-exempt obligations or a "related person" to such a user should consult his tax adviser concerning his qualification to receive exempt interest dividends should the Fund hold obligations financing such facility.

Interest on certain "private activity bonds" issued after August 7, 1986, although otherwise tax-exempt, is treated as a tax preference item for alternative minimum tax purposes. Under regulations to be promulgated, the Fund's exempt interest dividends will be treated the same way to the extent attributable to interest paid on such private activity bonds. Corporate shareholders should also be aware that the receipt of exempt interest dividends could subject them to alternative minimum tax under the provisions of Section 56(g) of the Code.

Some or all of the Fund's exempt interest dividends may be subject to state income taxes. The Fund will report to shareholders on a state by state basis the sources of its exempt interest dividends.

Since none of the Fund's income will consist of corporate dividends, no distributions will qualify for the 70% corporate dividends received deduction.

The Fund intends to distribute its net capital gains as capital gain dividends; such dividends are treated by shareholders as long-term capital gains. Such distributions will be designated as capital gain dividends by a written notice mailed to each shareholder no later than sixty days after the close of the Fund's taxable year. If a shareholder receives a capital gain dividend and holds his shares for six months or less, then any allowable loss on disposition of such shares will be treated as a long-term capital loss to the extent of such capital gain dividend.

Interest on indebtedness incurred or continued by shareholders to purchase or carry shares of the Fund will not be deductible for federal income tax purposes to the extent of the portion of the interest expense relating to exempt interest dividends; that portion is determined by multiplying the total amount of interest paid or accrued on the indebtedness by a fraction, the numerator of which is the exempt interest dividends received by a shareholder in his taxable year and the denominator of which is the sum of the exempt interest dividends and the taxable distributions out of the Fund's investment income and short-term capital gains received by the shareholder.

As mentioned above, at the end of each quarter at least 50% of the value of the Fund's assets must be invested in tax-exempt obligations in order for distributions to qualify as exempt interest dividends. Under particularly unusual circumstances, such as when the Fund is in a prolonged defensive investment position, it is possible that no portion of the Fund's distributions of income to its shareholders for a fiscal year would be exempt from federal income tax; however, the Fund does not presently anticipate that such unusual circumstances will occur.

For the fiscal year ended December 31, 1994, approximately 100% of the Fund's income distributions were designated as exempt from federal income taxes. The Fund advises its shareholders annually as to the federal tax status of all distributions made during the year.

The foregoing is only a summary of some of the important tax considerations generally affecting the Fund and its shareholders. No attempt is made to present a detailed explanation of the federal income tax treatment of the Fund or its shareholders, and this discussion is not intended as a substitute for careful tax planning. Accordingly, potential investors in the Fund are urged to consult their tax advisers with specific reference to their own tax situations.

FUND MANAGEMENT AND EXPENSES

FUND MANAGEMENT

Subject to the general supervision of the Fund's Board of Trustees, Keystone Management, located at 200 Berkeley Street, Boston, Massachusetts 02116-5034, serves as investment manager to the Fund and is responsible for the overall management of the Fund's business and affairs. Keystone Management, organized in 1989, is a wholly-owned subsidiary of Keystone, and its directors and principal executive officers have been affiliated with Keystone, a seasoned investment adviser, for a number of years. Keystone Management also serves as investment manager to each of the other funds in the Keystone Fund Family and to certain other funds in the Keystone Investments Family of Funds.

The Fund pays Keystone Management at the end of each calendar month a fee for its services consisting of (1) an amount calculated as set forth below:

Annual Management Fee	Income	Aggregate Net Asset Value of the Shares of the Fund
	2.0% of Gross Dividend and Interest Income Plus	
0.50% of the first		$100,000,000, plus
0.45% of the next		$100,000,000, plus
0.40% of the next		$100,000,000, plus
0.35% of the next		$100,000,000, plus
0.30% of the next		$100,000,000, plus
0.25% of amounts over		$500,000,000;

and (2) an amount equal to the amount of reimbursable expenses of Keystone Management accrued during such calendar month.

Pursuant to its Investment Management Agreement with the Fund (the "Management Agreement"), Keystone Management has delegated its investment management functions, except for certain administrative and management services, to Keystone and has entered into an Investment Advisory Agreement with Keystone (the "Investment Advisory Agreement"), under which Keystone provides investment advisory and management services to the Fund. Services performed by Keystone Management generally include (1) performing research and planning with respect to (a) the Fund's qualification as a regulated investment company under Subchapter M of the Code, (b) tax treatment of the Fund's portfolio investments, (c) tax treatment of special corporate actions (such as reorganizations), (d) state tax matters affecting the Fund, and (e) the Fund's distributions of income and capital gains; (2) preparing the Fund's federal and state tax returns; (3) providing services to the Fund's shareholders in connection with federal and state taxation and distributions of income and capital gains; and (4) storing documents relating to the Fund's activities.

Keystone, located at 200 Berkeley Street, Boston, Massachusetts 02116-5034, has provided investment advisory and management services to investment companies and private accounts since it was organized in 1932. Keystone is a wholly-owned subsidiary of Keystone Investments, Inc. (formerly Keystone Group, Inc.) ("Keystone Investments"), 200 Berkeley Street, Boston, Massachusetts 02116-5034.

Keystone Investments is a corporation predominantly owned by former and current members of management of Keystone and its affiliates. The shares of Keystone Investments common stock beneficially owned by management are held in a number of voting trusts, the trustees of which are George S. Bissell, Albert H. Elfner, III, Edward F. Godfrey and Ralph J. Spuehler, Jr. Keystone Investments provides accounting, bookkeeping, legal, personnel and general corporate services to Keystone Management, Keystone, their affiliates and the Keystone Investments Family of Funds.

Pursuant to the Investment Advisory Agreement, Keystone receives for its services an annual fee representing 85% of the management fee received by Keystone Management under the Management Agreement.

For the fiscal year ended December 31, 1994, the Fund paid or accrued to Keystone Management investment management fees of $5,941,545, which represented 0.43% of the Fund's average net assets. Of such amount paid to Keystone Management, $5,050,313 was paid to Keystone for its services to the Fund. In addition, the Fund reimbursed Keystone Management $2,029,000, which represented 0.14% of the Fund's average net assets, in connection with reimbursable expenses paid by Keystone Management on behalf of the Fund under the Management Agreement. For the fiscal year ended December 31, 1994, the total fee paid to Keystone Management by the Fund for investment management and administrative services fees was $7,970,545, which represented 0.57% of the Fund's average net assets.

Keystone, Keystone Management and the Fund have each adopted a Code of Ethics incorporating policies on personal securities trading as recommended by the Investment Company Institute.

FUND EXPENSES

In addition to the investment advisory and management fees discussed above, the principal expenses that the Fund is expected to pay include, but are not limited to, expenses of its transfer agent, its custodian and its independent auditors, expenses under its Distribution Plan, fees of its independent Trustees ("Independent Trustees"); expenses of shareholders' and Trustees' meetings, fees payable to government agencies, including registration and qualification fees of the Fund and its shares under federal and state securities laws, expenses of preparing, printing and mailing Fund prospectuses, notices, reports and proxy material and certain extraordinary expenses. In addition to such expenses, the Fund pays its brokerage commissions, interest charges and taxes. For the fiscal year ended December 31, 1994, the Fund paid 1.55% of its average net assets in expenses.

During the fiscal year ended December 31, 1994, the Fund paid or accrued to Keystone Investments $23,917 for certain accounting services and to Keystone Investor Resource Center, Inc. ("KIRC"), the Fund's transfer and dividend disbursing agent, $1,418,000 for certain transfer agent services. KIRC is a wholly-owned subsidiary of Keystone. The amount for transfer agent services is included in the amount of reimbursable expenses paid on behalf of the Fund by Keystone Management.

PORTFOLIO MANAGER

Betsy A. Blacher has been the Fund's Portfolio Manager since 1991. She is a Keystone Senior Vice President and Group Head and has more than 16 years of investment experience.

SECURITIES TRANSACTIONS

Keystone selects broker-dealers to execute transactions subject to the receipt of best execution. When selecting broker-dealers to execute portfolio transactions for the Fund, Keystone may follow a policy of considering as a factor the number of shares of the Fund sold by such broker-dealers. In addition, broker-dealers may, from time to time, be affiliated with the Fund, Keystone Management, Keystone, the Fund's principal underwriter or their affiliates.

PORTFOLIO TURNOVER

The Fund's portfolio turnover rates for the fiscal years ended December 31, 1994 and 1993 were 84% and 76%, respectively.

HOW TO BUY SHARES

Except as noted below the Fund generally offers its shares by direct investment only to those shareholders who already beneficially own shares of the Fund. The Fund also offers its shares through exchanges to shareholders of certain other funds in Keystone Investments Family of Funds. As previously mentioned, the Fund will be open however, to new investors during the Special Offering Period.

Shares of the Fund may be purchased from any broker-dealer that has a selling agreement with Keystone Investment Distributors Company (formerly named Keystone Distributors, Inc.) the Fund's principal underwriter ("Principal Underwriter"). The Principal Underwriter, a wholly-owned subsidiary of Keystone, is located at 200 Berkeley Street, Boston, Massachusetts 02116-5034.

Shares become entitled to income distributions declared on the first business day following receipt by the Fund's transfer agent of payment for the shares. It is the investor's responsibility to see that his dealer promptly forwards payment to the Principal Underwriter for shares being purchased through the dealer.

Orders for shares received by broker-dealers prior to that day's close of trading on the Exchange and transmitted to the Fund prior to its close of business that day will receive the offering price equal to the net asset value per share computed at the close of trading on the Exchange on the same day. Orders received by broker-dealers after that day's close of trading on the Exchange and transmitted to the Fund prior to the close of business on the next business day will receive the next business day's offering price. The initial purchase must be at least $10,000. During the Special Offering Period, the minimum initial investment will be $1,000. Purchase payments are fully invested at net asset value. There are no sales charges on purchases of Fund shares at the time of purchase.

CONTINGENT DEFERRED SALES CHARGE

With certain exceptions, when shares are redeemed within four calendar years after their purchase, a contingent deferred sales charge may be imposed at rates ranging from a maximum of 4% of amounts redeemed during the calendar year of purchase to 1% of amounts redeemed during the third calendar year after the year of purchase. No contingent deferred sales charge is imposed on amounts redeemed thereafter or on shares purchased through reinvestment of dividends and distributions. If imposed, the contingent deferred sales charge is deducted from the redemption proceeds otherwise payable to the shareholder. Since July 8, 1992, the contingent deferred sales charge attributable to shares purchased prior to January 1, 1992 has been retained by the Fund, and the contingent deferred sales charge attributable to shares purchased after January 1, 1992 is, to the extent permitted by NASD rules, paid to the Principal Underwriter. Accordingly, for the fiscal year ended December 31, 1994, the Fund retained $97,865 and the Principal Underwriter received $745,076, in deferred sales charges.

The contingent deferred sales charge is a declining percentage of the lesser of (1) the net asset value of the shares redeemed or (2) the total cost of such shares. No contingent deferred sales charge is imposed when a shareholder redeems amounts derived from (1) increases in the value of his account above the total cost of such shares due to increases in the net asset value per share of the Fund; (2) certain shares with respect to which the Fund did not pay a commission on issuance, including shares acquired through reinvestment of dividend income and capital gains distributions; or (3) shares held in all or part of more than four consecutive calendar years.

In determining whether a contingent deferred sales charge is payable and, if so, the percentage charge applicable, it is assumed that shares held the longest are the first to be redeemed. There is no deferred sales charge imposed on permitted exchanges of shares between Keystone funds that have adopted distribution plans pursuant to Rule 12b-1 under the 1940 Act. Moreover, when shares of one such fund have been exchanged for shares of another such fund, for purposes of any future contingent deferred sales charge, the calendar year of the purchase of the shares of the fund exchanged into is assumed to be the year shares tendered for exchange were originally purchased.

WAIVER OF DEFERRED SALES CHARGE

Shares also may be sold, to the extent permitted by applicable law, at net asset value without the payment of commissions or the imposition of a deferred sales charge upon redemption of Fund shares to (1) certain officers, Directors, Trustees and employees of the Fund, Keystone Management, Keystone and certain of their affiliates; (2) registered representatives of firms with dealer agreements with the Principal Underwriter; and (3) a bank or trust company acting as trustee for a single account.

In addition, no contingent deferred sales charge is imposed on a redemption of shares of the Fund in the event of (1) death or disability of the shareholder; (2) a lump sum distribution from a 401(k) plan or other benefit plan qualified under the Employee Retirement Income Security Act of 1974 ("ERISA"); (3) Automatic Withdrawals from ERISA plans if the shareholder is at least 59-1/2 years old; (4) involuntary redemptions of accounts having an aggregate net asset value of less than $1,000; (5) automatic withdrawals under an automatic withdrawal plan of up to 1 1/2% per month of the shareholder's initial account balance; (6) withdrawals consisting of loan proceeds to a retirement plan participant; (7) financial hardship withdrawals made by a retirement plan participant; or (8) withdrawals consisting of returns of excess contributions or excess deferral amounts made to a retirement plan participant.

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DISTRIBUTION PLAN

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The Fund bears some of the costs of selling its shares under a Distribution Plan adopted on June 1, 1983 pursuant to Rule 12b-1 under the 1940 Act. The Fund's Distribution Plan provides that the Fund may expend up to 0.3125% quarterly (approximately 1.25% annually) of average daily net asset value of its shares to pay distribution costs for sales of its shares and to pay shareholder service fees. The NASD currently limits such annual expenditures to 1%, of which 0.75% may be used to pay such distribution costs and 0.25% may be used to pay shareholder service fees. The aggregate amount that the Fund may pay for such distribution costs is limited to 6.25% of gross share sales since the inception of the Fund's Distribution Plan plus interest at the prime rate plus 1% on unpaid amounts thereof (less any contingent deferred sales charges paid by shareholders to the Principal Underwriter).

Payments under the Distribution Plan are currently made to the Principal Underwriter (which may reallow all or part to others such as dealers) (1) as commissions for Fund shares sold and (2) as shareholder service fees in respect to shares maintained by the recipients outstanding on the Fund's books for specified periods. Amounts paid or accrued to the Principal Underwriter under (1) and (2) in the aggregate may not exceed the annual limitations referred to above. The Principal Underwriter generally reallows to brokers or others a commission equal to 3% of the price paid for each Fund share sold as well as a shareholder service fee at a rate of 0.25% per annum of the net asset value of shares maintained by such recipients outstanding on the books of the Fund for specified periods.

During the Special Offering Period, the Principal Underwriter will reallow an increased commission equal to 4% of the price paid for each Fund share sold to those broker/dealers or others who allow their individual selling representatives to participate in the additional 1% commission. Broker/dealers or others not allowing their individual selling representatives to so participate will receive the normal 3% commission.

In connection with the reopening of the Fund during the Special Offering Period, the maximum annual expenditures permitted under the Fund's Distribution Plan have been temporarily fixed at 0.65% of the Fund's average daily net assets until such time as the Principal Underwriter shall have been fully paid all amounts due it that may have arisen from sales during the Special Offering Period. The Fund's Board of Trustees, in its sole discretion, may increase or otherwise modify or eliminate this temporary maximum percentage rate.

If the Fund is unable to pay the Principal Underwriter a commission on a new sale because the annual maximum has been reached, the Principal Underwriter intends, but is not obligated, to continue to accept new orders for the purchase of Fund shares and to pay or accrue commissions and service fees to dealers in excess of the amount it currently receives from the Fund. While the Fund is under no contractual obligation to pay the Principal Underwriter such amounts that exceed the Distribution Plan limitation, the Principal Underwriter intends to seek full payment of such charges from the Fund (together with interest at the rate of prime plus one percent) at such time in the future as, and to the extent that, payment thereof by the Fund would be within permitted limits. The Principal Underwriter currently intends to seek payment of interest only on such charges paid or accrued by the Principal Underwriter subsequent to July 7, 1992. If the Fund's Independent Trustees authorize such payments, the effect would be to extend the period of time during which the Fund incurs the maximum amount of costs allowed by the Distribution Plan. If the Distribution Plan is terminated, the Principal Underwriter will ask the Independent Trustees to take whatever action they deem appropriate under the circumstances with respect to payment of such amounts.

During the fiscal year ended December 31, 1994, the Fund recovered $97,865 in deferred sales charges. During the year, the Fund paid the Principal Underwriter $13,324,192 (0.98% of the Fund's average daily net asset value during the year) under the Distribution Plan. The amount paid by the Fund under its Distribution Plan, net of deferred sales charges, was $13,227,327 (0.97% of the Fund's average daily net asset value during the year). During the year, the Principal Underwriter received $9,126,418, after payments of commissions on new sales and service fees to dealers and others of $4,197,774.

The amounts and purposes of expenditures under the Distribution Plan must be reported to the Independent Trustees quarterly. The Independent Trustees may require or approve changes in the operation of the Distribution Plan and may require that total expenditures by the Fund under the Distribution Plan be kept within limits lower than the maximum amount permitted by the Distribution Plan as stated above. If such costs are not limited by the Independent Trustees, such costs could, for some period of time, be higher than such costs permitted by most other plans presently adopted by other investment companies.

The Distribution Plan may be terminated at any time by vote of the Fund's Independent Trustees or by vote of a majority of the outstanding voting shares of the Fund. Any change in the Distribution Plan that would materially increase the distribution expenses of the Fund provided for in the Distribution Plan requires shareholder approval. Otherwise, the Distribution Plan may be amended by votes of the majority of both (1) the Fund's Trustees and (2) the Independent Trustees, cast in person at a meeting called for the purpose of voting on such amendment.

While the Distribution Plan is in effect, the Fund is required to commit the selection and nomination of candidates for Independent Trustees to the discretion of the Independent Trustees.

Whether any expenditure under the Distribution Plan is subject to a state expense limit depends upon the nature of the expenditure and the terms of the state law, regulation or order imposing the limit. A portion of the Fund's Distribution Plan expenses may be includable in the Fund's total operating expenses for purposes of determining compliance with state expense limits.

ARRANGEMENTS WITH BROKER-DEALERS AND OTHERS

Upon written notice to dealers, the Principal Underwriter, at its own expense may periodically sponsor programs that offer additional compensation in connection with sales of Fund shares. Participation in such programs may be available to all dealers or to selected dealers who have sold or are expected to sell significant amounts of shares. Additional compensation may also include financial assistance to dealers in connection with preapproved seminars, conferences and advertising. No such programs or additional compensation will be offered to the extent they are prohibited by the laws of any state or any self-regulatory agency, such as the NASD.

The Principal Underwriter may, at its own expense, pay concessions in addition to those described above to dealers which satisfy certain criteria established from time to time by the Principal Underwriter. These conditions relate to increasing sales of shares of the Keystone funds over prior periods and certain other factors. Such payments may, depending on the dealer's satisfaction of the required conditions, be up to 0.25% of the value of shares sold by such dealer.

The Principal Underwriter may also pay a transaction fee (up to the level of payment allowed to dealers for the sale of shares, as described above) to banks and other financial service firms that facilitate transactions in shares of the Fund for their clients.

The Glass-Steagall Act currently limits the ability of a depository institution (such as a commercial bank or a savings and loan association) to become an underwriter or distributor of securities. In the event the Glass-Steagall Act is deemed to prohibit depository institutions from accepting payments under the arrangement described above, or should Congress relax current restrictions on depository institutions, the Board of Trustees will consider what action, if any, is appropriate.

In addition, state securities laws on this issue may differ from the interpretations of federal law expressed herein and banks and financial institutions may be required to register as dealers pursuant to state law.

HOW TO REDEEM SHARES

Fund shares may be redeemed for cash at the redemption value upon written order by the shareholder(s) to the Fund, c/o Keystone Investor Resource Center, Inc., Box 2121, Boston, Massachusetts 02106-2121, and presentation to the Fund of a properly endorsed share certificate if certificates have been issued. The signature(s) of the shareholder(s) on the written order and certificates must be guaranteed. The redemption value is the net asset value adjusted for fractions of a cent and may be more or less than the shareholder's cost depending upon changes in the value of the Fund's portfolio securities between purchase and redemption. A deferred sales charge may be imposed by the Fund at the time of redemption of certain shares as explained in "How to Buy Shares." If imposed, the deferred sales charge is deducted from the redemption proceeds otherwise payable to the shareholder.

At various times, the Fund may be requested to redeem shares for which it has not yet received good payment. In such a case the Fund will mail the redemption proceeds upon clearance of the purchase check, which may take up to 15 days or more. Any delay may be avoided by purchasing shares with a certified check drawn on a U.S. bank or by bank wire of funds. Although the mailing of a redemption check or the wiring of redemption proceeds may be delayed, the redemption value will be determined and the redemption processed in the ordinary course of business upon receipt of proper documentation. In such a case, after redemption and prior to the release of the proceeds, no appreciation or depreciation will occur in the value of the redeemed shares, and no interest will be paid on the redemption proceeds. If the mailing of a redemption has been delayed, the check will be mailed or the proceeds wired promptly after good payment has been collected.

The Fund computes the redemption value at the close of the Exchange at the end of the day on which it has received all proper documentation from the shareholder. Payment of the amount due on redemption, less any applicable deferred sales charge, will be made within seven days thereafter, except as noted above.

Shareholders also may redeem their shares through their broker-dealers. The Principal Underwriter, acting as agent for the Fund, stands ready to repurchase Fund shares upon orders from dealers as follows: redemption requests received by broker-dealers prior to that day's close of trading on the Exchange and transmitted to the Fund prior to its close of business that day will receive the net asset value per share computed at the close of trading on the Exchange on the same day. Redemption requests received by broker-dealers after that day's close of trading on the Exchange and transmitted to the Fund prior to the close of business on the next business day will receive the next business day's net asset value price. The Principal Underwriter will pay the redemption proceeds, less any applicable deferred sales charge, to the dealer placing the order within seven days thereafter, assuming it has received proper documentation. The Principal Underwriter charges no fees for this service, but the shareholder's broker-dealer may do so.

For the protection of shareholders, SIGNATURES ON CERTIFICATES, STOCK POWERS AND ALL WRITTEN ORDERS OR AUTHORIZATIONS MUST BE GUARANTEED BY A U.S. STOCK EXCHANGE MEMBER, A BANK OR OTHER PERSONS ELIGIBLE TO GUARANTEE SIGNATURES UNDER THE SECURITIES EXCHANGE ACT OF 1934 AND KIRC'S POLICIES. The Fund and KIRC may waive this requirement, but may also require additional documents in certain cases. Currently, the requirement for a signature guarantee has been waived on redemptions of $50,000 or less where the account address of record has been the same for a minimum period of 30 days. The Fund and KIRC reserve the right to withdraw this waiver at any time.

If the Fund receives a redemption or repurchase order, but the shareholder has not clearly indicated the amount of money or number of shares involved, the Fund cannot execute the order. In such cases, the Fund will request the missing information from the shareholder and process the order the day it receives such information.

TELEPHONE

Under ordinary circumstances, you may redeem up to $50,000 from your account by telephone by calling toll free 1-800-343-2898. To engage in telephone transactions generally, you must complete the appropriate sections of the Fund's application.

In order to insure that instructions received by KIRC are genuine when you initiate a telephone transaction, you will be asked to verify certain criteria specific to your account. At the conclusion of the transaction, you will be given a transaction number confirming your request, and written confirmation of your transaction will be mailed the next business day. Your telephone instructions will be recorded. Redemptions by telephone are allowed only if the address and bank account of record have been the same for a minimum period of 30 days. If you cannot reach the Fund by telephone, you should follow the procedures for redeeming by mail or through a broker as set forth above.

SMALL ACCOUNTS

Because of the high cost of maintaining small accounts, the Fund reserves the right to redeem your account if its value has fallen below $1,000, the current minimum investment level, as a result of your redemptions (but not as a result of market action). You will be notified in writing and allowed 60 days to increase the value of your account to the minimum investment level. No deferred sales charges are applied to such redemptions.

REDEMPTIONS IN KIND

If conditions arise that would make it undesirable for the Fund to pay for all redemptions in cash, the Fund may authorize payment to be made in portfolio securities or other property. The Fund has obligated itself, however, under the 1940 Act to redeem for cash all shares of the Fund presented for redemption by any one shareholder in any 90 day period up to the lesser of $250,000 or 1% of the Fund's net assets at the beginning of such period. Securities delivered in payment of redemptions would be valued at the same value assigned to them in computing the net asset value per share and would, to the extent permitted by law, be readily marketable. Shareholders receiving such securities would incur brokerage costs when these securities are sold.

GENERAL

The Fund reserves the right, at any time, to terminate, suspend or change the terms of any redemption method described in this prospectus, except redemption by mail, and to impose fees.

Except as otherwise noted, neither the Fund, KIRC nor the Principal Underwriter assumes responsibility for the authenticity of any instructions received by any of them from a shareholder in writing, over the Keystone Automated Response Line ("KARL") or by telephone. KIRC will employ reasonable procedures to confirm that instructions received over KARL or by telephone are genuine. Neither the Fund, KIRC nor the Principal Underwriter will be liable when following instructions received over KARL or by telephone that KIRC reasonably believes to be genuine.

The Fund may temporarily suspend the right to redeem its shares when (1) the Exchange is closed, other than customary weekend and holiday closings; (2) trading on the Exchange is restricted; (3) an emergency exists and the Fund cannot dispose of its investments or fairly determine their value; or (4) the Securities and Exchange Commission so orders.

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SHAREHOLDER SERVICES
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Details on all shareholder services may be obtained from KIRC, by writing or by calling toll free 1-800-343-2898.

KEYSTONE AUTOMATED RESPONSE LINE

KARL offers you specific fund account information and price and yield quotations as well as the ability to effect account transactions, including investments, exchanges and redemptions. You may access KARL by dialing toll-free 1-800-346-3858 on any touch-tone telephone, 24 hours a day, seven days a week.

EXCHANGES

A shareholder who has obtained the appropriate prospectus may exchange shares of the Fund for shares of certain funds in the Keystone Fund Family, Keystone Precious Metals Holdings, Inc., ("KPMH"), Keystone International Fund Inc. ("KIF"), Keystone Tax Exempt Trust ("KTET") or Keystone Liquid Trust ("KLT") on the basis of their respective net asset values by calling toll free 1-800-343-2898 or by writing KIRC at Box 2121, Boston, Massachusetts 02106-2121. (See "How to Redeem Shares" for additional information on telephone transactions.)

Fund shares purchased by check may be exchanged for shares of the named funds, other than KPMH or KTET, after 15 days. In order to exchange Fund shares for shares of KPMH or KTET, a shareholder must have held Fund shares for a period of at least six months. There is a $10.00 exchange fee for each exchange; however, there is no fee for exchange orders received by the Fund from an individual shareholder over KARL. If the shares being tendered for exchange have been held for less than four years and are still subject to a deferred sales charge, such charge will carry over to the shares being acquired in the exchange transaction. The Fund reserves the right, after providing the required notice to shareholders, to terminate this exchange offer or to change its terms, including the right to change the fee for any exchange.

Orders to exchange shares of the Fund for shares of KLT will be executed by redeeming the shares of the Fund and purchasing shares of KLT at the net asset value of KLT shares determined after the proceeds from such redemption become available, which may be up to seven days after such redemption. In all other cases, orders for exchanges received by the Fund prior to 4:00 p.m. eastern time on any day the funds are open for business will be executed at the respective net asset values determined as of the close of business that day. Orders for exchanges received after 4:00 p.m. eastern time on any business day will be executed at the respective net asset values determined at the close of the next business day.

An excessive number of exchanges may be disadvantageous to the Fund. Therefore, the Fund, in addition to its right to reject any exchange, reserves the right to terminate the exchange privilege of any shareholder who makes more than five exchanges of shares of the funds in a year or three in a calendar quarter.

An exchange order must comply with the requirements for a redemption or repurchase order and must specify the dollar value or number of shares to be exchanged. Exchanges are subject to the minimum initial purchase requirements of the fund being acquired. An exchange constitutes a sale for federal income tax purposes.

The exchange privilege is available only in states where shares of the fund being acquired may legally be sold.

AUTOMATIC WITHDRAWAL PLAN

Under an Automatic Withdrawal Plan, shareholders may arrange for regular monthly or quarterly fixed withdrawal payments. Each payment must be at least $100 and may be as much as 1% per month or 3% per quarter of the total net asset value of the Fund shares in the shareholder's account when the Automatic Withdrawal Plan is opened. Fixed withdrawal payments are not subject to a deferred sales charge. Excessive withdrawals may decrease or deplete the value of a shareholder's account.

OTHER SERVICES

Under certain circumstances shareholders may, within 30 days after a redemption, reinstate their accounts at current net asset value.

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PERFORMANCE DATA

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From time to time, the Fund may advertise "total return," "current yield" and "tax equivalent yield." ALL FIGURES ARE BASED ON HISTORICAL EARNINGS AND ARE NOT INTENDED TO INDICATE FUTURE PERFORMANCE. Total return refers to the Fund's average annual compounded rates of return over specified periods determined by comparing the initial amount invested to the ending redeemable value of that amount. The resulting equation assumes reinvestment of all dividends and distributions and deduction of all recurring charges applicable to all shareholder accounts. The deduction of the contingent deferred sales charge is reflected in the applicable years. The exchange fee is not included in the calculation.

Current yield quotations represent the yield on an investment for a stated 30-day period computed by dividing net investment income earned per share during the base period by the maximum offering price per share on the last day of the base period.

Tax equivalent yield is, in general, the current yield divided by a factor equal to one minus a stated income tax rate and reflects the yield a taxable investment would have to achieve in order to equal on an after-tax basis a tax exempt yield.

The Fund may also include comparative performance and general mutual fund industry information in advertising or marketing the Fund's shares, such as data from Lipper Analytical Services, Inc., Morningstar, Inc., CDS- Weisenberger and Value Line or other financial and industry publications.

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FUND SHARES

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The Fund currently issues one class of shares, which participate equally in dividends and distributions and have equal voting, liquidation and other rights. When issued and paid for, the shares will be fully paid and nonassessable by the Fund. Shares may be exchanged as explained under "Shareholder Services," but will have no other preference, conversion, exchange or preemptive rights. Shares are redeemable, transferable and freely assignable as collateral. There are no sinking fund provisions. The Fund may establish additional classes or series of shares.

Shareholders of the Fund are entitled to one vote for each full share owned and fractional votes for fractional shares. The Fund will have special meetings from time to time as required under its Declaration of Trust and under the 1940 Act. As provided in the Fund's Declaration of Trust, shareholders have the right to remove Trustees by an affirmative vote of two-thirds of the outstanding shares. A special meeting of the shareholders will be held when 10% of the outstanding shares request a meeting for the purpose of removing a Trustee. As prescribed by Section 16(c) of the 1940 Act, shareholders may be eligible for shareholder communication assistance in connection with the special meeting.

Under Massachusetts law it is possible that a Fund shareholder may be held personally liable for the Fund's obligations. However, the Fund's Declaration of Trust provides that shareholders shall not be subject to any personal liability for the Fund's obligations and provides indemnification from Fund assets for any shareholder held personally liable for the Fund's obligations. Disclaimers of such liability are included in each Fund agreement.

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ADDITIONAL INFORMATION

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KIRC, located at 101 Main Street, Cambridge, Massachusetts 02142-1515, is a wholly owned subsidiary of Keystone and serves as the Fund's transfer agent and dividend disbursing agent.

When the Fund determines from its records that more than one account in the Fund is registered in the name of a shareholder or shareholders having the same address, upon written notice to those shareholders the Fund intends, when an annual report or semi-annual report of the Fund is required to be furnished, to mail one copy of such report to that address.

Except as otherwise stated in this prospectus or required by law, the Fund reserves the right to change the terms of the offer stated in this prospectus without shareholder approval, including the right to impose or change fees for services provided.

ADDITIONAL INVESTMENT INFORMATION

CORPORATE AND MUNICIPAL BOND RATINGS

S&P CORPORATE AND MUNICIPAL BOND RATINGS

A. MUNICIPAL NOTES

An S&P note rating reflects the liquidity concerns and market access risks unique to notes. Notes due in three years or less will likely receive a note rating. Notes maturing beyond three years will most likely receive a long-term debt rating. The following criteria are used in making that assessment:

1. amortization schedule (the larger the final maturity relative to other maturities the more likely it will be treated as a note); and

2. source of payment (the more dependent the issue is on the market for its refinancing, the more likely it will be treated as a note).

Note ratings are as follows:

1. SP-1 -- Strong capacity to pay principal and interest. Those issues determined to possess a very strong capacity to pay debt service are given a plus (+) designation.

2. SP-2 -- Satisfactory capacity to pay principal and interest, with some vulnerability to adverse financial and economic changes over the terms of the notes.

3. SP-3 -- Speculative capacity to pay principal and interest.

B. TAX EXEMPT DEMAND BONDS

S&P assigns "dual" ratings to all long-term debt issues that have as part of their provisions a demand or double feature.

The first rating addresses the likelihood of repayment of principal and interest as due, and the second rating addresses only the demand feature. The long-term debt rating symbols are used for bonds to denote the long-term maturity and the commercial paper rating symbols are used to denote the put option (for example, "AAA/A-1+"). For the newer "demand notes," S&P note rating symbols, combined with the commercial paper symbols, are used (for example, "SP - -- 1+/A-1+").

C. CORPORATE AND MUNICIPAL BOND RATINGS

An S&P corporate or municipal bond rating is a current assessment of the creditworthiness of an obligor, including obligors outside the U.S., with respect to a specific obligation. This assessment may take into consideration obligors such as guarantors, insurers or lessees. Ratings of foreign obligors do not take into account currency exchange and related uncertainties. The ratings are based on current information furnished by the issuer or obtained by S&P from other sources it considers reliable.

The ratings are based, in varying degrees, on the following considerations:

1. likelihood of default capacity and willingness of the obligor as to the timely payment of interest and repayment of principal in accordance with the terms of the obligation;

2. nature of and provisions of the obligation; and

3. protection afforded by and relative position of the obligation in the event of bankruptcy, reorganization or other arrangement under the laws of bankruptcy and other laws affecting creditors' rights.

PLUS (+) OR MINUS (-): To provide more detailed indications of credit quality, ratings from "AA" to "BBB" may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories.

A provisional rating is sometimes used by S&P. It assumes the successful completion of the project being financed by the debt being rated and indicates that payment of debt service requirements is largely or entirely dependent upon the successful and timely completion of the project. This rating, however, while addressing credit quality subsequent to completion of the project, makes no comment on the likelihood of, or the risk of default upon, failure of such completion.

D. BOND RATINGS

Bond ratings are as follows:

1. AAA -- Debt rated AAA has the highest rating assigned by S&P. Capacity to pay interest and repay principal is extremely strong.

2. AA -- Debt rated AA has a very strong capacity to pay interest and repay principal and differs from the higher rated issues only in small degree.

3. A -- Debt rated A has a strong capacity to pay interest and repay principal although it is somewhat more susceptible to the adverse effects of changes in circumstances and economic conditions than debt in higher rated categories.

4. BBB -- Debt rated BBB is regarded as having an adequate capacity to pay interest and repay principal. Whereas it normally exhibits adequate protection parameters, adverse economic conditions or changing circumstances are more likely to lead to a weakened capacity to pay interest and repay principal for debt in this category than in higher rated categories.

MOODY'S CORPORATE AND MUNICIPAL BOND RATINGS

A. MUNICIPAL NOTES

A Moody's rating for municipal short-term obligations will be designated Moody's Investment Grade or ("MIG"). These ratings recognize the difference between short-term credit risk and long-term risk. Factors affecting the liquidity of the borrower and the short-term cyclical elements are critical in short-term ratings.

A short-term rating may also be assigned on issues with a demand feature -- variable rate demand obligation ("VRDO"). Such ratings will be designated as VMIG. Short-term ratings on issues with demand features are differentiated by the use of the VMIG symbol to reflect such characteristics as payment upon periodic demand rather than fixed maturity dates and payment relying on the external liquidity.

The note ratings are as follows:

1. MIG1/VMIG1 This designation denotes the best quality. There is present strong protection by established cash flows, superior liquidity support or demonstrated broadbased access to the market for refinancing.

2. MIG2/VMIG2 This designation denotes high quality. Margins of protection are ample although not so large as in the preceding group.

3. MIG3/VMIG3 This designation denotes favorable quality. All security elements are accounted for but there is lacking the undeniable strength of the preceding grades. Liquidity and cash flow protection may be narrow and market access for refinancing is likely to be less well established.

4. MIG4/VMIG4 This designation denotes adequate quality. Protection commonly regarded as required of an investment security is present and although not distinctly or predominantly speculative, there is specific risk.

B. CORPORATE AND MUNICIPAL BOND RATINGS

1. Aaa -- Bonds rated Aaa are judged to be of the best quality. They carry the smallest degree of investment risk and are generally referred to as "gilt-edge." Interest payments are protected by a large or by an exceptionally stable margin and principal is secure. While the various protective elements are likely to change, such changes as can be visualized are most unlikely to impair the fundamentally strong position of such issues.

2. Aa -- Bonds rated Aa are judged to be of high quality by all standards. Together with the Aaa group, they comprise what are generally known as high grade bonds. They are rated lower than the best bonds because margins of protection may not be as large as in Aaa securities or fluctuation of protective elements may be of greater amplitude or there may be other elements present that make the long term risks appear somewhat larger than in Aaa securities.

3. A -- Bonds rated A possess many favorable investment attributes and are to be considered as upper medium grade obligations. Factors giving security to principal and interest are considered adequate, but elements may be present that suggest a susceptibility to impairment sometime in the future.

4. Baa -- Bonds rated Baa are considered to be medium grade obligations, i.e., they are neither highly protected nor poorly secured. Interest payments and principal security appear adequate for the present, but certain protective elements may be lacking or may be characteristically unreliable over any great length of time. Such bonds lack outstanding investment characteristics and in fact have speculative characteristics as well.

Moody's applies numerical modifiers, 1, 2 and 3 in each generic rating classification from Aa through Baa in its corporate bond rating system. The modifier 1 indicates that the security ranks in the higher end of its generic rating category; the modifier 2 indicates a mid-range ranking; and the modifier 3 indicates that the issue ranks in the lower end of its generic rating category.

Con. (--) -- Municipal bonds for which the security depends upon the completion of some act or the fulfillment of some condition are rated conditionally. These are bonds secured by (1) earnings of projects under construction, (2) earnings of projects unseasoned in operation experience, (3) rentals that begin when facilities are completed, or (4) payments to which some other limiting condition attaches. Parenthetical rating denotes probable credit stature upon completion of construction or elimination of basis of condition.

Those municipal bonds in the Aa, A, and Baa groups that Moody's believes possess the strongest investment attributes are designated by the symbols Aa 1, A 1, and Baa 1.

FITCH CORPORATE AND MUNICIPAL RATINGS

A. MUNICIPAL NOTES

Fitch's short-term ratings apply to debt obligations that are payable on demand or have original maturities of generally three years or less. These include commercial paper, certificates of deposit, medium-term notes, and municipal and investment notes. The short-term rating places greater emphasis on the existence of liquidity necessary to meet the issuer's obligations in a timely manner.

The note ratings are as follows:

1. F-1+ Exceptionally Strong Credit Quality. Issues assigned this rating are regarded as having the strongest degree of assurance for timely payment.

2. F-1 Very Strong Credit Quality. Issues assigned this rating reflect an assurance of timely payment only slightly less in degree than issues rated F-1+.

3. F-2 Good Credit Quality. Issues assigned this rating have a satisfactory degree of assurance for timely payment, but the margin of safety is not as great as for issues assigned the two higher ratings.

4. F-3 Fair Credit Quality. Issues assigned this rating have characteristics suggesting that the degree of assurance for timely payment is adequate, however, near-term adverse changes could cause these securities to be rated below investment grade.

B. CORPORATE AND MUNICIPAL BOND RATINGS

AAA -- Bonds considered to be investment grade and of the highest credit quality. The obligor has an exceptionally strong ability to pay interest and repay principal, which is unlikely to be affected by reasonably foreseeable events.

AA -- Bonds considered to be investment grade and of very high credit quality. The obligor's ability to pay interest and repay principal is very strong, although not quite as strong as bonds rated AAA.

A -- Bonds considered to be investment grade and of high credit quality. The obligor's ability to pay interest and repay principal is considered to be strong, but may be more vulnerable to adverse changes in economic conditions and circumstances than bonds with higher ratings.

BBB -- Bonds considered to be investment grade and of satisfactory credit quality. The obligor's ability to pay interest and repay principal is considered to be adequate. Adverse changes in economic conditions and circumstances, however, are more likely to have adverse impact on these bonds, and therefore impair timely payment. The likelihood that the ratings of these bonds will fall below investment grade is higher than for bonds with higher ratings.

PLUS (+) OR MINUS (-) signs are used with a rating symbol to indicate the relative position of a credit within the rating category. Plus and minus signs, however, are not used in the AAA category.

A CONDITIONAL rating is premised on the successful completion of a project or the occurrence of a specific event.

Debt rated BB, B, CCC, CC and C by S&P is regarded, on balance, as predominantly speculative with respect to capacity to pay interest and repay principal in accordance with the terms of the obligation. BB indicates the lowest degree of speculation and C the highest degree of speculation. While such debt will likely have some quality and protective characteristics, these are outweighed by large uncertainties or major risk exposures to adverse conditions. Debt rated C1 by S&P is debt (income bonds) on which no interest is being paid. Debt rated D by S&P is in default and payment of interest and/or repayment of principal is in arrears. Bonds that are rated Caa by Moody's are of poor standing. Such issues may be in default or there may be present elements of danger with respect to principal or interest. Bonds that are rated Ca by Moody's represent obligations that are speculative in a high degree. Such issues are often in default or have other market shortcomings. Bonds that are rated C by Moody's are the lowest rated bonds, and issues so rated can be regarded as having extremely poor prospects of ever attaining any real investment standing. Debt rated BB, B, CCC, CC, and C by Fitch is regarded as speculative with respect to capacity to pay interest and repay principal in accordance with the terms of the obligation. BB indicates the lowest degree of speculation and C represents the highest degree of speculation. Debt rated DDD, DD, and D are in default on interest and/or principal payments.

DESCRIPTIONS OF CERTAIN TYPES OF INVESTMENTS AND INVESTMENT TECHNIQUES AVAILABLE TO THE FUND

OBLIGATIONS OF FOREIGN BRANCHES OF UNITED STATES BANKS

The obligations of foreign branches of U.S. banks may be general obligations of the parent bank in addition to the issuing branch, or may be limited by the terms of a specific obligation and by government regulation. Payment of interest and principal upon these obligations may also be affected by governmental action in the country of domicile of the branch (generally referred to as sovereign risk). In addition, evidences of ownership of such securities may be held outside the U.S. and the Fund may be subject to the risks associated with the holding of such property overseas. Examples of governmental actions would be the imposition of currency controls, interest limitations, withholding taxes, seizure of assets or the declaration of a moratorium. Various provisions of federal law governing domestic branches do not apply to foreign branches of domestic banks.

OBLIGATIONS OF UNITED STATES BRANCHES OF FOREIGN BANKS

Obligations of U.S. branches of foreign banks may be general obligations of the parent bank in addition to the issuing branch, or may be limited by the terms of a specific obligation and by federal and state regulation as well as by governmental action in the country in which the foreign bank has its head office. In addition, there may be less publicly available information about a U.S. branch of a foreign bank than about a domestic bank.

MASTER DEMAND NOTES

Master demand notes are unsecured obligations that permit the investment of fluctuating amounts by the Fund at varying rates of interest pursuant to direct arrangements between the Fund, as lender, and the issuer as borrower. Master demand notes may permit daily fluctuations in the interest rate and daily changes in the amounts borrowed. The Fund has the right to increase the amount under the note at any time up to the full amount provided by the note agreement, or to decrease the amount. The borrower may repay up to the full amount of the note without penalty. Notes acquired by the Fund permit the Fund to demand payment of principal and accrued interest at any time (on not more than seven days' notice). Notes acquired by the Fund may have maturities of more than one year, provided that (1) the Fund is entitled to payment of principal and accrued interest upon not more than seven days notice, and (2) the rate of interest on such notes is adjusted automatically at periodic intervals which normally will not exceed 31 days, but may extend up to one year. The notes will be deemed to have a maturity equal to the longer of the period remaining to the next interest rate adjustment or the demand notice period. Because these types of notes are direct lending arrangements between the lender and borrower, such instruments are not normally traded and there is no secondary market for these notes, although they are redeemable and thus repayable by the borrower at face value plus accrued interest at any time. Accordingly, the Fund's right to redeem is dependent on the ability of the borrower to pay principal and interest on demand. In connection with master demand note arrangements, Keystone considers, under standards established by the Board of Trustees, earning power, cash flow and other liquidity ratios of the borrower and will monitor the ability of the borrower to pay principal and interest on demand. These notes are not typically rated by credit rating agencies. Unless rated, the Fund may invest in them only if at the time of an investment the issuer meets the criteria established for commercial paper discussed in the statement of additional information.

REPURCHASE AGREEMENTS

The Fund may enter into repurchase agreements with member banks of the Federal Reserve System having at least $1 billion in assets, primary dealers in U.S. government securities or other financial institutions believed by Keystone to be creditworthy. Such persons must be registered as U.S. government securities dealers with appropriate regulatory organizations. Under such agreements, the bank, primary dealer or other financial institution agrees upon entering into the contract to repurchase the security at a mutually agreed upon date and price, thereby determining the yield during the term of the agreement. This results in a fixed rate of return insulated from market fluctuations during such period. Under a repurchase agreement, the seller must maintain the value of the securities subject to the agreement at not less than the repurchase price, such value being determined on a daily basis by marking the underlying securities to their market value. Although the securities subject to the repurchase agreement might bear maturities exceeding a year, the Fund only intends to enter into repurchase agreements that provide for settlement within a year and usually within seven days. Securities subject to repurchase agreements will be held by the Fund's custodian or in the Federal Reserve book entry system. The Fund does not bear the risk of a decline in the value of the underlying security unless the seller defaults under its repurchase obligation. In the event of a bankruptcy or other default of a seller of a repurchase agreement, the Fund could experience both delays in liquidating the underlying securities and losses, including (1) possible declines in the value of the underlying securities during the period while the Fund seeks to enforce its rights thereto; (2) possible subnormal levels of income and lack of access to income during this period; and (3) expenses of enforcing its rights. The Board of Trustees has established procedures to evaluate the creditworthiness of each party with whom the Fund enters into repurchase agreements by setting guidelines and standards of review for Keystone and monitoring Keystone's actions with regard to repurchase agreements.

REVERSE REPURCHASE AGREEMENTS

Under a reverse repurchase agreement, the Fund would sell securities and agree to repurchase them at a mutually agreed upon date and price. The Fund intends to enter into reverse repurchase agreements to avoid otherwise having to sell securities during unfavorable market conditions in order to meet redemptions. At the time the Fund enters into a reverse repurchase agreement, it will establish a segregated account with the Fund's custodian containing liquid assets such as U.S. government securities or other high grade debt securities having a value not less than the repurchase price (including accrued interest) and will subsequently monitor the account to ensure such value is maintained. Reverse repurchase agreements involve the risk that the market value of the securities that the Fund is obligated to repurchase may decline below the repurchase price. Borrowing and reverse repurchase agreements magnify the potential for gain or loss on the portfolio securities of the Fund and, therefore, increase the possibility of fluctuation in the Fund's net asset value. Such practices may constitute leveraging. In the event the buyer of securities under a reverse repurchase agreement files for bankruptcy or becomes insolvent, such buyer or its trustee or receiver may receive an extension of time to determine whether to enforce the Fund's obligation to repurchase the securities and the Fund's use of the proceeds of the reverse repurchase agreement may effectively be restricted pending such determination. The staff of the Securities and Exchange Commission ("SEC") has taken the position that the 1940 Act treats reverse repurchase agreements as being included in the percentage limit on borrowings imposed on a fund.

"WHEN ISSUED" SECURITIES

The Fund may also purchase and sell securities and currencies on a when issued and delayed delivery basis. When issued or delayed delivery transactions arise when securities or currencies are purchased or sold by the Fund with payment and delivery taking place in the future in order to secure what is considered to be an advantageous price and yield to the Fund at the time of entering into the transaction. When the Fund engages in when issued and delayed delivery transactions, the Fund relies on the buyer or seller, as the case may be, to consummate the sale. Failure to do so may result in the Fund missing the opportunity to obtain a price or yield considered to be advantageous. When issued and delayed delivery transactions may be expected to occur a month or more before delivery is due. However, no payment or delivery is made by the Fund until it receives payment or delivery from the other party to the transaction. A separate account of liquid assets equal to the value of such purchase commitments will be maintained until payment is made. When issued and delayed delivery agreements are subject to risks from changes in value based upon changes in the level of interest rates, currency rates and other market factors, both before and after delivery. The Fund does not accrue any income on such securities or currencies prior to their delivery. To the extent the Fund engages in when issued and delayed delivery transactions, it will do so consistent with its investment objective and policies and not for the purpose of investment leverage.

LOANS OF SECURITIES TO BROKER-DEALERS

The Fund may lend securities to brokers and dealers pursuant to agreements requiring that the loans be continuously secured by cash or securities of the U.S. government, its agencies or instrumentalities, or any combination of cash and such securities, as collateral equal at all times in value to at least the market value of the securities loaned. Such securities loans will not be made with respect to the Fund if as a result the aggregate of all outstanding securities loans exceeds 15% of the value of the Fund's total assets taken at their current value. The Fund continues to receive interest or dividends on the securities loaned and simultaneously earns interest on the investment of the cash loan collateral in U.S. Treasury notes, certificates of deposit, other high-grade, short-term obligations or interest bearing cash equivalents. Although voting rights attendant to securities loaned pass to the borrower, such loans may be called at any time and will be called so that the securities may be voted by the Fund if, in the opinion of the Fund, a material event affecting the investment is to occur. There may be risks of delay in receiving additional collateral or in recovering the securities loaned or even loss of rights in the collateral should the borrower of the securities fail financially. Loans may only be made to borrowers deemed to be of good standing, under standards approved by the Board of Trustees, when the income to be earned from the loan justifies the attendant risks.

DERIVATIVES

The Fund may use derivatives in furtherance of its investment objective. Derivatives are financial contracts whose value depends on, or is derived from, the value of an underlying asset, reference rate or index. These assets, rates, and indices may include bonds, stocks, mortgages, commodities, interest rates, currency exchange rates, bond indices and stock indices. Derivatives can be used to earn income or protect against risk, or both. For example, one party with unwanted risk may agree to pass that risk to another party who is willing to accept the risk, the second party being motivated, for example, by the desire either to earn income in the form of a fee or premium from the first party, or to reduce its own unwanted risk by attempting to pass all or part of that risk to the first party.

Derivatives can be used by investors such as the Fund to earn income and enhance returns, to hedge or adjust the risk profile of the portfolio, and either in place of more traditional direct investments or to obtain exposure to otherwise inaccessible markets. The Fund is permitted to use derivatives for one or more of these purposes. Each of these uses entails greater risk than if derivatives were used solely for hedging purposes. The Fund uses futures contracts and related options for hedging purposes. Derivatives are a valuable tool which, when used properly, can provide significant benefit to Fund shareholders. Keystone is not an aggressive user of derivatives with respect to the Fund. However, the Fund may take positions in those derivatives that are within its investment policies if, in Keystone's judgement, this represents an effective response to current or anticipated market conditions. Keystone's use of derivatives is subject to continuous risk assessment and control from the standpoint of the Fund's investment objective and policies.

Derivatives may be (1) standardized, exchange-traded contracts or (2) customized, privately negotiated contracts. Exchange-traded derivatives tend to be more liquid and subject to less credit risk than those that are privately negotiated.

There are four principal types of derivative instruments -- options, futures, forwards and swaps -- from which virtually any type of derivative transaction can be created. Further information regarding options and futures, is provided later in this section and is provided in the Fund's statement of additional information.

Debt instruments that incorporate one or more of these building blocks for the purpose of determining the principal amount of and/or rate of interest payable on the debt instruments are often referred to as "structured securities." An example of this type of structured security is indexed commercial paper. The term is also used to describe certain securities issued in connection with the restructuring of certain foreign obligations. See "Structured Securities" below. The term "derivative" is also sometimes used to describe securities involving rights to a portion of the cash flows from an underlying pool of mortgages or other assets from which payments are passed through to the owner of, or that collateralize, the securities.

While the judicious use of derivatives by experienced investment managers such as Keystone can be beneficial, derivatives also involve risks different from, and, in certain cases, greater than, the risks presented by more traditional investments. Following is a general discussion of important risk factors and issues concerning the use of derivatives that investors should understand before investing in the Fund.

* Market Risk -- This is the general risk attendant to all investments that the value of a particular investment will decline or otherwise change in a way detrimental to the Fund's interest.

* Management Risk -- Derivative products are highly specialized instruments that require investment techniques and risk analyses different from those associated with stocks and bonds. The use of a derivative requires an understanding not only of the underlying instrument, but also of the derivative itself, without the benefit of observing the performance of the derivative under all possible market conditions. In particular, the use and complexity of derivatives require the maintenance of adequate controls to monitor the transactions entered into, the ability to assess the risk that a derivative adds to the Fund's portfolio and the ability to forecast price, interest rate or currency exchange rate movements correctly.

* Credit Risk -- This is the risk that a loss may be sustained by the Fund as a result of the failure of another party to a derivative (usually referred to as a "counterparty") to comply with the terms of the derivative contract. The credit risk for exchange traded derivatives is generally less than for privately negotiated derivatives, since the clearing house, which is the issuer or counterparty to each exchange-traded derivative, provides a guarantee of performance. This guarantee is supported by a daily payment system (i.e., margin requirements) operated by the clearing house in order to reduce overall credit risk. For privately negotiated derivatives, there is no similar clearing agency guarantee. Therefore, the Fund considers the creditworthiness of each counterparty to a privately negotiated derivative in evaluating potential credit risk.

* Liquidity Risk -- Liquidity risk exists when a particular instrument is difficult to purchase or sell. If a derivative transaction is particularly large or if the relevant market is illiquid (as is the case with many privately negotiated derivatives), it may not be possible to initiate a transaction or liquidate a position at an advantageous price.

* Leverage Risk -- Since many derivatives have a leverage component, adverse changes in the value or level of the underlying asset, rate or index can result in a loss substantially greater than the amount invested in the derivative itself. In the case of swaps, the risk of loss generally is related to a notional principal amount, even if the parties have not made any initial investment. Certain derivatives have the potential for unlimited loss, regardless of the size of the initial investment.

* Other Risks -- Other risks in using derivatives include the risk of mispricing or improper valuation and the inability of derivatives to correlate perfectly with underlying assets, rates and indices. Many derivatives, in particular privately negotiated derivatives, are complex and often valued subjectively. Improper valuations can result in increased cash payment requirements to counterparties or a loss of value to a Fund. Derivatives do not always perfectly or even highly correlate or track the value of the assets, rates or indices they are designed to closely track. Consequently, the Fund's use of derivatives may not always be an effective means of, and sometimes could be counterproductive to, furthering the Fund's investment objective.

OPTIONS TRANSACTIONS

WRITING COVERED OPTIONS. The Fund may write (i.e., sell) covered call and put options. By writing a call option, the Fund becomes obligated during the term of the option to deliver the securities underlying the option upon payment of the exercise price. By writing a put option, the Fund becomes obligated during the term of the option to purchase the securities underlying the option at the exercise price if the option is exercised. The Fund also may write straddles (combinations of covered puts and calls on the same underlying security).

The Fund may only write "covered" options. This means that so long as the Fund is obligated as the writer of a call option, it will own the underlying securities subject to the option or, in the case of call options on U.S. Treasury bills, the Fund might own substantially similar U.S. Treasury bills. If the Fund has written options against all of its securities which are available for writing options, the Fund may be unable to write additional options unless it sells a portion of its portfolio holdings to obtain new securities against which it can write options. If this were to occur, higher portfolio turnover and correspondingly greater brokerage commissions and other transaction costs may result. However, the Fund does not expect that this will occur.

The Fund will be considered "covered" with respect to a put option it writes if, so long as it is obligated as the writer of the put option, it deposits and maintains with its custodian in a segregated account liquid assets having a value equal to or greater than the exercise price of the option.

The principal reason for writing call or put options is to obtain, through a receipt of premiums, a greater current return than would be realized on the underlying securities alone. The Fund receives a premium from writing a call or put option, which it retains whether or not the option is exercised. By writing a call option, the Fund might lose the potential for gain on the underlying security while the option is open, and by writing a put option the Fund might become obligated to purchase the underlying security for more than its current market price upon exercise.

PURCHASING OPTIONS. The Fund may purchase put or call options, including purchasing put or call options for the purpose of offsetting previously written put or call options of the same series.

If the Fund is unable to effect a closing purchase transaction with respect to covered options it has written, the Fund will not be able to sell the underlying security or dispose of assets held in a segregated account until the options expire or are exercised.

An option position may be closed out only in a secondary market for an option of the same series. Although the Fund generally will write only those options for which there appears to be an active secondary market, there is no assurance that a liquid secondary market will exist for any particular option at any particular time, and for some options no secondary market may exist. In such event, it might not be possible to effect a closing transaction in a particular option.

Options on some securities are relatively new, and it is impossible to predict the amount of trading interest that will exist in such options. There can be no assurance that viable markets will develop or continue. The failure of such markets to develop or continue could significantly impair the Fund's ability to use such options to achieve its investment objective.

OPTIONS TRADING MARKETS. Options in which the Fund will trade generally are listed on national securities exchanges. Exchanges on which such options currently are traded include the Chicago Board Options Exchange and the New York, American, Pacific and Philadelphia Stock Exchanges. Options on some securities may not be listed on any Exchange, but traded in the over-the-counter market. Options traded in the over-the-counter market involve the additional risk that securities dealers participating in such transactions could fail to meet their obligations to the Fund. The use of options traded in the over-the-counter market may be subject to limitations imposed by certain state securities authorities. In addition to the limits on its use of options discussed herein, the Fund is subject to the investment restrictions described in this prospectus and in the statement of additional information.

The staff of the SEC is of the view that the premiums that the Fund pays for the purchase of unlisted options, and the value of securities used to cover unlisted options written by the Fund, are considered to be invested in illiquid securities or assets for the purpose of calculating whether the Fund is in compliance with its investment restriction relating to illiquid investments.

FUTURES TRANSACTIONS

The Fund may enter into currency and other financial futures contracts and write options on such contracts. The Fund intends to enter into such contracts and related options for hedging purposes. The Fund will enter into futures on securities or currencies or index-based futures contracts in order to hedge against changes in interest or exchange rates or securities prices. A futures contract on securities or currencies is an agreement to buy or sell securities or currencies at a specified price during a designated month. A futures contract on a securities index does not involve the actual delivery of securities, but merely requires the payment of a cash settlement based on changes in the securities index. The Fund does not make payment or deliver securities upon entering into a futures contract. Instead, it puts down a margin deposit, which is adjusted to reflect changes in the value of the contract and which continues until the contract is terminated.

The Fund may sell or purchase futures contracts. When a futures contract is sold by the Fund, the value of the contract will tend to rise when the value of the underlying securities or currencies declines and to fall when the value of such securities or currencies increases. Thus, the Fund sells futures contracts in order to offset a possible decline in the value of its securities or currencies. If a futures contract is purchased by the Fund, the value of the contract will tend to rise when the value of the underlying securities or currencies increases and to fall when the value of such securities or currencies declines. The Fund intends to purchase futures contracts in order to establish what is believed by Keystone to be a favorable price and rate of return for securities or favorable exchange rate for currencies the Fund intends to purchase.

The Fund also intends to purchase put and call options on futures contracts for hedging purposes. A put option purchased by the Fund would give it the right to assume a position as the seller of a futures contract. A call option purchased by the Fund would give it the right to assume a position as the purchaser of a futures contract. The purchase of an option on a futures contract requires the Fund to pay a premium. In exchange for the premium, the Fund becomes entitled to exercise the benefits, if any, provided by the futures contract, but is not required to take any action under the contract. If the option cannot be exercised profitably before it expires, the Fund's loss will be limited to the amount of the premium and any transaction costs.

The Fund may enter into closing purchase and sale transactions in order to terminate a futures contract and may sell put and call options for the purpose of closing out its options positions. The Fund's ability to enter into closing transactions depends on the development and maintenance of a liquid secondary market. There is no assurance that a liquid secondary market will exist for any particular contract or at any particular time. As a result, there can be no assurance that the Fund will be able to enter into an offsetting transaction with respect to a particular contract at a particular time. If the Fund is not able to enter into an offsetting transaction, the Fund will continue to be required to maintain the margin deposits on the contract and to complete the contract according to its terms, in which case it would continue to bear market risk on the transaction.

Although futures and options transactions are intended to enable the Fund to manage market, interest rate or exchange rate risk, unanticipated changes in interest rates, exchange rates or market prices could result in poorer performance than if it had not entered into these transactions. Even if Keystone correctly predicts interest or exchange rate movements, a hedge could be unsuccessful if changes in the value of the Fund's futures position did not correspond to changes in the value of its investments. This lack of correlation between the Fund's futures and securities or currencies positions may be caused by differences between the futures and securities or currencies markets or by differences between the securities or currencies underlying the Fund's futures position and the securities or currencies held by or to be purchased for the Fund. Keystone will attempt to minimize these risks through careful selection and monitoring of the Fund's futures and options positions.

The Fund does not intend to use futures transactions for speculation or leverage. The Fund has the ability to write options on futures, but intends to write such options only to close out options purchased by the Fund. The Fund will not change these policies without supplementing the information in its prospectus and statement of additional information.

FOREIGN CURRENCY TRANSACTIONS

As discussed above, if permitted by its investment policies, the Fund may invest in securities of foreign issuers. When the Fund invests in foreign securities they usually will be denominated in foreign currencies, and the Fund temporarily may hold funds in foreign currencies. Thus, the value of Fund shares will be affected by changes in exchange rates.

As one way of managing exchange rate risk, in addition to entering into currency futures contracts, the Fund may enter into forward currency exchange contracts (agreements to purchase or sell currencies at a specified price and date). The exchange rate for the transaction (the amount of currency the Fund will deliver or receive when the contract is completed) is fixed when the Fund enters into the contract. The Fund usually will enter into these contracts to stabilize the U.S. dollar value of a security it has agreed to buy or sell. The Fund intends to use these contracts to hedge the U.S. dollar value of a security it already owns, particularly if the Fund expects a decrease in the value of the currency in which the foreign security is denominated. Although the Fund will attempt to benefit from using forward contracts, the success of its hedging strategy will depend on Keystone's ability to predict accurately the future exchange rates between foreign currencies and the U.S. dollar. The value of the Fund's investments denominated in foreign currencies will depend on the relative strength of those currencies and the U.S. dollar, and the Fund may be affected favorably or unfavorably by changes in the exchange rates or exchange control regulations between foreign currencies and the dollar. Changes in foreign currency exchange rates also may affect the value of dividends and interest earned, gains and losses realized on the sale of securities and net investment income and gains, if any, to be distributed to shareholders by the Fund. The Fund may also purchase and sell options related to foreign currencies in connection with hedging strategies.

VARIABLE AND FLOATING RATE INSTRUMENTS. Fixed-income securities may have fixed, variable or floating rates of interest. Variable and floating rate securities pay interest at rates that are adjusted periodically, according to a specified formula. A "variable" interest rate adjusts at predetermined intervals (e.g., daily, weekly or monthly), while a "floating" interest rate adjusts whenever a specified benchmark rate (such as the bank prime lending rate) changes.

If permitted by its investment policies the Fund may invest in fixed-income securities that pay interest at a coupon rate equal to a base rate, plus additional interest for a certain period of time if short-term interest rates rise above a predetermined level or "cap." The amount of such an additional interest payment typically is calculated under a formula based on a short-term interest rate index multiplied by a designated factor.

INVERSE FLOATING RATE SECURITIES. If permitted by its investment policies, the Fund may also invest in securities with rates that move inversely to market rates ("inverse floaters"). An inverse floater bears an interest rate that resets in the opposite direction of the change in a specified interest rate index. As market interest rates rise, the interest rate on the inverse floater goes down, and vice versa. Inverse floaters tend to exhibit greater price volatility than fixed-rate bonds of similar maturity and credit quality. The interest rates on inverse floaters may be significantly reduced, even to zero, if interest rates rise. Moreover, the secondary market for inverse floaters may be limited in rising interest rate environments.

An inverse floater may be considered to be leveraged to the extent that its interest rate varies by a magnitude that exceeds the magnitude of the change in the index rate of interest. The higher degree of leverage inherent in inverse floaters is associated with greater volatility in market value.

STRUCTURED SECURITIES. Structured securities generally represent interests in entities organized and operated solely for the purpose of restructuring the investment characteristics of debt obligations. This type of restructuring involves the deposit with or purchase by an entity, such as a corporation or trust, of specified instruments (such as commercial bank loans) and the issuance by that entity of one or more classes of structured securities backed by, or representing interests in, the underlying instruments. The cash flow on the underlying instruments may be apportioned among the newly issued structured securities to create securities with different investment characteristics such as varying maturities, payment priorities and interest rate provisions, and the extent of the payments made with respect to structured securities is dependent on the extent of the cash flow on the underlying instruments. Because structured securities typically involve no credit enhancement, their credit risk generally will be equivalent to that of the underlying instruments. Structured securities of a given class may be either subordinated or unsubordinated to the right of payment of another class. Subordinated structured securities typically have higher yields and present greater risks than unsubordinated structured securities.

KEYSTONE
FUND FAMILY

Quality Bond Fund (B-1)

Diversified Bond Fund (B-2)

High Income Bond Fund (B-4)

Balanced Fund (K-1)

Strategic Growth Fund (K-2)

Growth and Income Fund (S-1)

Mid-Cap Growth Fund (S-3)

Small Company Growth
Fund (S-4)

International Fund

Precious Metals Holdings

Tax Free Fund

Tax Exempt Trust

Liquid Trust

[LOGO] KEYSTONE
INVESTMENTS
200 Berkeley Street
Boston, Massachusetts 02116-5034 [Recycle Logo]

KEYSTONE

[Photo of Mother with Infant on Porch]

TAX FREE
FUND

[LOGO]

PROSPECTUS AND
APPLICATION

KEYSTONE TAX FREE FUND

PART B

STATEMENT OF ADDITIONAL INFORMATION

KEYSTONE TAX FREE FUND

STATEMENT OF ADDITIONAL INFORMATION

APRIL 28, 1995

This statement of additional information is not a prospectus, but relates to, and should be read in conjunction with, the prospectus of Keystone Tax Free Fund dated April 28, 1995. A copy of the prospectus may be obtained from Keystone Investment Distributors Company (formerly known as Keystone Distributors, Inc.) the Fund's principal underwriter, ("Principal Underwriter"), 200 Berkeley Street, Boston, Massachusetts 02116-5034 or your broker-dealer.

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THE FUND'S OBJECTIVE AND POLICIES

The Fund's investment objective is to provide shareholders with the highest possible current income, exempt from federal income taxes, while preserving capital. The Fund invests primarily in municipal bonds, but also may invest in certain other securities as described in the Appendix hereto and the

"Additional Investment Information" section of the Fund's prospectus.

FUNDAMENTAL NATURE OF INVESTMENT OBJECTIVE

The investment objective of the Fund is fundamental and may not be changed without approval of the holders of a majority, as defined in the Investment Company Act of 1940 (the "1940 Act"), of the Fund's outstanding shares (which means the lesser of (1) 67% of the shares represented at a meeting at which more than 50% of the outstanding shares are represented or (2) more than 50% of the outstanding shares).

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INVESTMENT RESTRICTIONS

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None of the restrictions enumerated in this paragraph may be changed without a vote of the holders of a 1940 Act majority of the Fund's outstanding shares. The Fund will not do the following:

(1) purchase securities on margin, but the Fund may obtain such short-term credits as may be necessary for the clearance of purchases and sales of securities;

(2) make short sales of securities or maintain a short position, unless at all times when a short position is open it owns an equal amount of such securities or of securities that without payment of any further consideration are convertible into or exchangeable for securities of the same issue as, and equal in amount to, the securities sold short;

(3) borrow money, except that the Fund may (a) borrow money from banks for emergency or extraordinary purposes in aggregate amounts up to one-third of its net assets, and (b) enter into reverse repurchase agreements;

(4) pledge, mortgage or hypothecate its assets except to secure indebtedness permitted by subparagraph (3) above, with pledged assets to be no more than 15% of its total assets; the Fund understands that pledges in excess of approximately 6% of its net assets would result in its inability to sell additional shares in one state; however, the Fund has no present intention of exceeding this limit;

(5) purchase any security other than United States ("U.S.") government securities of any issuer if as a result more than 25% of its total assets would be invested in a single industry, including industrial development bonds from the same facility or similar types of facilities; governmental issuers of municipal bonds are not regarded as members of an industry and the Fund may invest more than 25% of its assets in industrial development bonds;

(6) purchase any security, other than U.S. government securities, if as a result more than 5% of the Fund's total assets would be invested in securities of the issuer, or the Fund would hold more than 10% of the voting securities of the issuer;

(7) invest for the purpose of exercising control over or management of any company;

(8) invest in securities of other investment companies, except as part of a merger, consolidation, purchase of assets or similar transaction approved by the Fund's shareholders;

(9) purchase or sell commodities or commodity contracts or real estate, except that it may purchase and sell securities secured by real estate and securities of companies that invest in real estate, and may engage in currency or other financial futures and related options transactions;

(10) act as an underwriter except to the extent that, in connection with the disposition of its portfolio investments, it may be deemed to be an underwriter under federal securities laws; or purchase securities that are not readily marketable except for repurchase agreements;

(11) purchase or retain securities of an issuer if, to the knowledge of the Fund, an officer, Trustee or Director of the Fund or Keystone owns beneficially more than 1/2 of 1% of the shares or securities of such issuer and all such officers, Trustees and Directors owning more than 1/2 of 1% of such shares or securities together own more than 5% of such shares or securities;

(12) purchase securities of any issuer if the person responsible for payment, together with any predecessor, has been in operation for less than three years if, as a result, the aggregate of such investments would exceed 5% of the Fund's total assets; provided, however, that this restriction shall not apply to U.S. government securities or to any obligation the payment of which involves the credit and taxing power of any person authorized to issue municipal bonds;

(13) invest in interests in oil, gas or other mineral exploration or

development programs;

(14) make loans, except to the extent that the purchase of debt instruments or repurchase agreements may be deemed to be loans; repurchase agreements maturing in more than seven days will not exceed 10% of the Fund's total assets; and

(15) purchase securities of foreign issuers.

The foregoing percentage restrictions will apply at the time of the purchase of a security and shall not be considered violated unless an excess or deficiency occurs or exists immediately after and as a result of a purchase of such security. For the purpose of limitations (5) and (6), the Fund will treat each state, territory and possession of the U.S., the District of Columbia and, if its assets and revenues are separate from those of the entity or entities creating it, each political subdivision, agency and instrumentality of any one (or more, as in the case of a multistate authority or agency) of the foregoing as an issuer of all securities that are backed primarily by its assets or revenues; each company as an issuer of all securities that are backed primarily by its assets or revenues; and each of the foregoing entities as an issuer of all securities that it guarantees; provided, however, that for the purpose of limitation (6) no entity shall be deemed to be an issuer of a security that it guarantees so long as no more than 10% of the Fund's total assets (taken at current value) are invested in securities guaranteed by the entity and securities of which it is otherwise deemed to be an issuer.

The Fund does not presently intend to invest more than 25% of its total assets in (1) municipal bonds of a single state and its subdivisions, agencies and instrumentalities; of a single territory or possession of the U.S. and its subdivisions, agencies or instrumentalities; or of the District of Columbia and any subdivision, agency or instrumentality thereof; or (2) municipal bonds the payment of which depends on revenues derived from a single facility or similar types of facilities. Since certain municipal bonds may be related in such a way that an economic, business or political development or change affecting one such security could likewise affect the other securities, a change in this policy could result in increased investment risk, but no change is presently contemplated. The Fund may invest more than 25% of its total assets in industrial development bonds.

Notwithstanding limitation 8 or any of the other limitations above, the Fund may invest all of its assets in the securities of a single open-end management investment company with substantially the same fundamental investment objectives, policies, and restrictions as the Fund. See "Fund Objective and Policies" in the prospectus.

VALUATION OF SECURITIES

The Fund believes that reliable market quotations generally are not readily available for purposes of valuing municipal bonds. As a result, depending on the particular municipal bonds owned by the Fund, it is likely that most of the valuations for such bonds will be based upon their fair value determined under procedures that have been approved by the Board of Trustees. Non-tax exempt securities for which market quotations are readily available are valued on a consistent basis at that price quoted that, in the opinion of the Board of Trustees or the person designated by the Board of Trustees to make the determination, most nearly represents the market value of the particular security. Short-term investments that are purchased with maturities of sixty days or less are valued at amortized cost (original purchase cost as adjusted for amortization of premium or accretion of discount), which, when combined with accrued interest, approximates market; short-term investments maturing in more than sixty days for which market quotations are readily available are valued at current market value; and short-term investments maturing in more than sixty days when purchased that are held on the sixtieth day prior to maturity are valued at amortized cost (market value on the sixtieth day adjusted for amortization of premium or accretion of discount), which, when combined with accrued interest, approximates market and which, in any case, reflects fair value as determined by the Board of Trustees. All other investments are valued at market value or, where market quotations are not readily available, at fair value as determined in good faith using methods prescribed by the Fund's Board of Trustees.

SALES CHARGES

In order to reimburse the Fund for certain expenses relating to the sale of its shares (see "Distribution Plan"), a contingent deferred sales charge may be imposed at the time of redemption of certain Fund shares within four calendar years after their purchase. If imposed, the contingent deferred sales charge is deducted from the redemption proceeds otherwise payable to the shareholder. Since July 8, 1992, the deferred sales charge attributable to shares purchased prior to January 1, 1992 has been retained by the Fund, and the deferred sales charge attributable to shares purchased after January 1, 1992 is, to the extent permitted by the National Association of Securities Dealers, Inc. ("NASD") rules, paid to the Principal Underwriter. Accordingly, for the fiscal year ended December 31, 1994, the Fund retained $97,865 and the Principal Underwriter received $745,076 in deferred sales charges.

The contingent deferred sales charge is a declining percentage of the lesser of (1) the net asset value of the shares redeemed or (2) the total cost of such shares. No contingent deferred sales charge is imposed when the shareholder redeems amounts derived from (1) increases in the value of his account above the total cost of such shares due to increases in the net asset value per share of the Fund; (2) certain shares with respect to which the Fund did not pay a commission on issuance, including shares acquired through reinvestment of dividend income and capital gains distributions; or (3) shares held in all or part of more than four consecutive calendar years.

Subject to the limitations stated above, the Fund imposes a contingent deferred sales charge according to the following schedule: 4% of amounts redeemed during the calendar year of purchase; 3% of amounts redeemed during the calendar year after the year of purchase; 2% of amounts redeemed during the second calendar year after the year of purchase; and 1% of amounts redeemed during the third calendar year after the year of purchase. No contingent deferred sales charge is imposed on amounts redeemed thereafter.

The following example will illustrate the operation of the contingent deferred sales charge. Assume that an investor makes a purchase payment of $10,000 during the calendar year 1995 and on a given date in 1996 the value of the investor's account has grown through investment performance and reinvestment of distributions to $12,000. On such date in 1996, the investor could redeem up to $2,000 ($12,000 minus $10,000) without incurring a deferred sales charge. If, on such date, the investor should redeem $3,000, a deferred sales charge would be imposed on $1,000 of the redemption (the amount by which the investor's account was reduced by the redemption below the amount of the initial purchase payment). The charge would be imposed at the rate of 3% because the redemption is made during the calendar year after the calendar year of purchase, for a total deferred sales charge of $30.

In determining whether a contingent deferred sales charge is payable and, if so, the percentage charge applicable, it is assumed that shares held the longest are the first to be redeemed. There is no contingent deferred sales charge imposed on permitted exchanges of shares between funds in the Keystone Investments Family of Funds that have adopted distribution plans pursuant to Rule 12b-1 under the 1940 Act. Moreover, when shares of one such fund have been exchanged for shares of another such fund, for purposes of any future contingent deferred sales charge, the calendar year of the purchase of the shares of the fund exchanged into is assumed to be the year shares tendered for exchange were originally purchased.

Shares also may be sold, to the extent permitted by applicable law, regulations, interpretations or exemptions, at net asset value without the imposition of a deferred sales charge upon redemption of shares to (1) officers, Directors, Trustees, full-time employees and sales representatives of Keystone Management, Inc. ("Keystone Management"), Keystone Investment Management Company (formerly known as Keystone Custodian Funds, Inc.) ("Keystone"), Keystone Investments, Inc. (formerly known as Keystone Group, Inc.) ("Keystone Investments"), Harbor Capital Management Company, Inc., their subsidiaries and the Principal Underwriter who have been such for not less than ninety days; and (2) the pension and profit-sharing plans established by said companies, their subsidiaries and affiliates, for the benefit of their officers, Directors, Trustees, full-time employees and sales representatives, provided all such sales are made upon the written assurance of the purchaser that the purchase is made for investment purposes and that the securities will not be resold except through redemption by the Fund.

In addition, no contingent deferred sales charge is imposed on a redemption of shares of the Fund purchased by a bank or trust company in a single account in the name of such bank or trust company as trustee, if the initial investment in shares of the Fund, any fund in the Keystone Fund Family, Keystone Precious Metals Holdings, Inc., Keystone International Fund Inc., Keystone Tax Exempt Trust, Keystone Liquid Trust and/or any fund in the Keystone America Fund Family is at least $500,000 and any commission paid by the Fund and such other funds at the time of such purchase is not more than 1% of the amount invested.

In addition, no contingent deferred sales charge is imposed on a redemption of shares of the Fund in the event of (1) death or disability of the shareholder; (2) a lump sum distribution from a 401(k) plan or other benefit plan qualified under the employee Retirement Income Security Act of 1974 ("ERISA"); (3) automatic withdrawals from ERISA plans if the shareholder is at least 59-1/2 years old; (4) involuntary redemptions of accounts having an aggregate net asset value of less than $1,000; (5) automatic withdrawals under an automatic withdrawal plan of up to 1-1/2% per month of the shareholder's initial account balance; (6) withdrawals consisting of loan proceeds to a retirement plan participant; (7) financial hardship withdrawals made by a retirement plan participant; or (8) withdrawals consisting of returns of excess contributions or excess deferral amounts made to a retirement plan participant.

DISTRIBUTION PLAN

Rule 12b-1 under the 1940 Act permits investment companies, such as the Fund, to use their assets to bear expenses of distributing their shares if they comply with various conditions, including adoption of a distribution plan containing certain provisions set forth in Rule 12b-1. On January 19, 1983, the Fund's Distribution Plan described below was approved by the Fund's Board of Trustees, including a majority of the Trustees who are not interested persons of the Fund as defined in the 1940 Act ("Independent Trustees") and the Trustees who have no direct or indirect financial interest in the Distribution Plan or any agreement related thereto (the "Rule 12b-1 Trustees" who are the same as the Independent Trustees). On May 27, 1983, the Distribution Plan was approved by the Fund's shareholders, and it became effective on June 1, 1983.

The Fund's Distribution Plan provides that the Fund may expend up to 0.3125% quarterly (approximately 1.25% annually) of average daily net asset value of its shares to pay distribution costs for sales of its shares and to pay shareholder service fees. The NASD currently limits such annual expenditures to 1%, of which 0.75% may be used to pay such distribution costs and 0.25% may be used to pay shareholder service fees. The aggregate amount that the Fund may pay for such distribution costs is limited to 6.25% of gross share sales since the inception of the Fund's Distribution Plan plus interest at the prime rate plus 1% on unpaid amounts thereof (less any contingent deferred sales charge paid by shareholders to the Principal Underwriter). The Fund operates its Distribution Plan in accordance with both the Distribution Plan and the NASD rules.

In connection with the Distribution Plan, Fund shares are offered for sale at net asset value without any initial sales charge, and the Fund pays or accrues to the Principal Underwriter a commission for each sale. Specifically, payments under the Distribution Plan are currently made to the Principal Underwriter (which may reallow all or part to others such as dealers) (1) as commissions for Fund shares sold and (2) as shareholder service fees in respect to shares maintained by the recipients outstanding on the Fund's books for specified periods. Amounts paid or accrued to the Principal Underwriter under (1) and (2) in the aggregate may not exceed the annual limitations referred to above. The Principal Underwriter generally reallows to brokers or others a commission equal to 3% of the price paid for each Fund share sold as well as a shareholder service fee at a rate of 0.25% per annum of the net asset value of shares maintained by such recipients outstanding on the books of the Fund for specified periods. Such commissions and service fees are included in the Fund's operating expenses.

Beginning May 1, 1995 until July 31, 1995 or until the Fund attains $50,000,000 in aggregate sales whichever occurs first, (the "Special Offering Period"), the Fund will reopen to new investors. During the Special Offering Period, the Principal Underwriter will reallow to those brokers or others an increased commission equal to 4% of the price paid for each Fund share sold who allow their individual selling representatives to participate in the additional 1% commission.

In connection with the reopening of the Fund during the Special Offering Period, the maximum annual expenditures permitted under the Fund's Distribution Plan have been temporarily fixed at 0.65% of the Fund's average daily net assets until such time as the Principal Underwriter shall have been fully paid all amounts due Keystone that may have arisen from sales during the Special Offering Period. The Fund's Board of Trustees, in its sole discretion, may increase or otherwise modify or eliminate the temporary maximum percentage rate.

If the Fund is unable to pay the Principal Underwriter a commission on a new sale because the annual maximum has been reached, the Principal Underwriter intends, but is not obligated, to continue to accept new orders for the purchase of Fund shares and to pay commissions and service fees to dealers in excess of the amount it currently receives from the Fund. While the Fund is under no contractual obligation to reimburse the Principal Underwriter for advances made by the Principal Underwriter in excess of the Distribution Plan limitation, the Principal Underwriter intends to seek full payment of such charges from the Fund (together with interest at the rate of prime plus one percent) at such time in the future as, and to the extent that, payment thereof by the Fund would be within permitted limits. The Principal Underwriter currently intends to seek payment of interest only on such charges paid or accrued by the Principal Underwriter subsequent to July 7, 1992. If the Independent Trustees authorize such payments, the effect will be to extend the period of time during which the Fund incurs the maximum amount of costs allowed by the Distribution Plan. The Independent Trustees have agreed to cause the Fund to reimburse the Principal Underwriter such portion of this amount at such future time when the payment of such amounts would not cause the Fund to exceed the Distribution Plan limitation. If the Distribution Plan is terminated, the

Principal Underwriter will ask the Independent Trustees to take whatever action they deem appropriate under the circumstances with respect to payment of such amounts.

The total amounts paid by the Fund under the foregoing arrangements may not exceed the maximum Distribution Plan limit specified above, and the amounts and purposes of expenditures under the Distribution Plan must be reported to the Fund's Rule 12b-1 Trustees quarterly. The Fund's Rule 12b-1 Trustees may require or approve changes in the implementation or operation of the Distribution Plan, and may also require that total expenditures by the Fund under the Distribution Plan be kept within limits lower than the maximum amount permitted by the Distribution Plan as stated above. If such costs are not limited by the Independent Trustees, such costs could, for some period of time, be higher than such costs permitted by most other plans presently adopted by other investment companies.

The Distribution Plan may be terminated at any time by vote of the Rule 12b-1 Trustees, or by vote of a majority of the outstanding voting securities of the Fund. Any change in the Distribution Plan that would materially increase the distribution expenses of the Fund provided for in the Distribution Plan requires shareholder approval. Otherwise, the Distribution Plan may be amended by the Trustees, including the Fund's Rule 12b-1 Trustees.

While the Distribution Plan is in effect, the Fund will be required to commit the selection and nomination of candidates for Independent Trustees to the discretion of the Independent Trustees.

The Fund is subject to certain state annual expense limitations, the most restrictive of which is as follows:

> 2.5% of the first $30 million of Fund average net assets; 2.0% of the next $70 million of Fund average net assets; and 1.5% of Fund average net assets over $100 million.

Capital charges and certain expenses, including a portion of the Fund's Distribution Plan expenses, are not included in the calculation of the state expense limitations. This limitation may be modified or eliminated in the future.

Whether any expenditure under the Distribution Plan is subject to a state expense limit will depend upon the nature of the expenditure and the terms of the state law, regulation or order imposing the limit. Any expenditure subject to such a limit will be included in the Fund's total operating expenses for purposes of determining compliance with the expense limit. A portion of the Fund's Distribution Plan expenses may be includable in the Fund's total operating expenses for purposes of determining compliance with state expense limits.

The Independent Trustees of the Fund have determined that the sales of the Fund's shares resulting from payments under the Distribution Plan have benefited the Fund.

PRINCIPAL UNDERWRITER

Pursuant to a Principal Underwriting Agreement (the "Underwriting Agreement"), Keystone Investment Distributors Company acts as the Fund's principal underwriter. The Principal Underwriter, located at 200 Berkeley Street, Boston, Massachusetts 02116-5034, is a Delaware corporation wholly-owned by Keystone. The Principal Underwriter, as agent, has agreed to use its best efforts to find purchasers for the shares. The Principal Underwriter may retain and employ representatives to promote distribution of the shares and may obtain orders from brokers, dealers and others, acting as principals, for sales of shares to them. The Underwriting Agreement provides that the Principal Underwriter will bear the expense of preparing, printing and distributing advertising and sales literature and prospectuses used by it. In its capacity as principal underwriter, the Principal Underwriter may receive payments from the Fund pursuant to the Fund's Distribution Plan.

The Underwriting Agreement provides that it will remain in effect as long as its terms and continuance are approved by a majority of the Fund's Independent Trustees at least annually at a meeting called for that purpose and if its continuance is approved annually by vote of a majority of Trustees or by vote of a majority of the outstanding shares.

The Underwriting Agreement may be terminated, without penalty, on 60 days' written notice by the Board of Trustees or by a vote of a majority of outstanding shares. The Underwriting Agreement will terminate automatically upon its "assignment" as that term is defined in the 1940 Act.

From time to time, if in the Principal Underwriter's judgment it could benefit the sales of Fund shares, the Principal Underwriter may use its discretion in providing to selected dealers promotional materials and selling aids, including, but not limited to, personal computers, related software and Fund data files.

For the fiscal years ended December 31, 1992 and 1993 the Principal Underwriter earned commissions of $7,972,003 and $4,969,409 (amount represents commissions earned during the fiscal year ended December 31, 1993 and excludes recapture by the Principal Underwriter during said fiscal year of $4,272,087 in advances made during previous fiscal years), respectively, after paying commissions of $7,260,876 and $3,705,342 (amount represents sales commissions only and excludes $3,661,327 in maintenance fees paid during the fiscal year), respectively, to retail dealers under the Distribution Plan. During the fiscal year ended December 31, 1994, the Fund paid the Principal Underwriter $13,324,192 under the Distribution Plan. The amount paid by the Fund under its Distribution Plan, net of deferred sales charges, was $13,226,327 (0.97% of the Fund's average daily net asset value during the period). During the year, the Principal Underwriter received $9,126,418 after payments of commissions on new sales and service fees to dealers and others of $4,197,774. See the "Distribution Plan".

TRUSTEES AND OFFICERS

The Trustees of the Fund, their principal occupations and some of their affiliations over the last five years, and the officers of the Fund are as follows:

*ALBERT H. ELFNER, III: President, Trustee and Chief Executive Officer of the Fund; Chairman of the Board, President, Director and Chief Executive Officer of Keystone Investments; President and Trustee or Director of Keystone Capital Preservation and Income Fund, Keystone Intermediate Term Bond Fund, Keystone Strategic Income Fund, Keystone World Bond Fund, Keystone Tax Free Income Fund, Keystone State Tax Free Fund, Keystone State Tax Free Fund-Series II, Keystone Fund for Total Return, Keystone Global Opportunities Fund, Keystone Hartwell Emerging Growth Fund, Inc., Keystone Hartwell Growth Fund, Inc., Keystone Omega Fund, Inc., Keystone Fund of the Americas-Luxembourg and Keystone Fund of the Americas-U.S., Keystone Strategic Development Fund (collectively, "Keystone America Fund Family"); Keystone Quality Bond Fund (B-1), Keystone Diversified Bond Fund (B-2), Keystone High Income Bond Fund (B-4), Keystone Balanced Fund (K-1), Keystone Strategic Growth Fund (K-2), Keystone Growth and Income Fund (S-1), Keystone Mid-Cap Growth Fund (S-3), Keystone Small Company Growth Fund (S-4); Keystone International Fund, Keystone Precious Metals Holdings, Inc., Keystone Tax Exempt Trust, Keystone Liquid Trust (together with the Fund, collectively, "Keystone Fund Family"); Keystone Institutional Adjustable Rate Fund and Master Reserves Trust (all such funds, collectively, "Keystone Investments Family of Funds"); Director and Chairman of the Board, Chief Executive Officer and Vice Chairman of Keystone; Chairman of the Board and Director of Keystone Institutional Company, Inc. ("Keystone Institutional") and Keystone Fixed Income Advisors ("KFIA"); Director, Chairman of the Board, Chief Executive Officer and President of Keystone Management and Keystone Software Inc. ("Keystone Software"); Director and President of Hartwell Keystone Advisers, Inc. ("Hartwell Keystone"), Keystone Asset Corporation, Keystone Capital Corporation, and Keystone Trust Company; Director of the Principal Underwriter, Keystone Investor Resource Center, Inc. ("KIRC"), and Fiduciary Investment Company, Inc. ("FICO"); Director and Vice President of Robert Van Partners, Inc.; Director of Boston Children's Services Association; Trustee of Anatolia College, Middlesex School, and Middlebury College; Member, Board of Governors of New England Medical Center; and former Trustee of Neworld Bank.

FREDERICK AMLING: Trustee of the Fund; Trustee or Director of all other funds in the Keystone Investments Family of Funds; Professor, Finance Department, George Washington University; President, Amling & Company (investment advice); Member, Board of Advisers, Credito Emilano (banking); and former Economics and Financial Consultant, Riggs National Bank.

CHARLES A. AUSTIN III: Trustee of the Fund; Trustee or Director of all other funds in the Keystone Investments Family of Funds; Investment Counselor to Appleton Partners, Inc.; former Managing Director, Seaward Management Corporation (investment advice); and former Director, Executive Vice President and Treasurer, State Street Research & Management Company (investment advice).

*GEORGE S. BISSELL: Chairman of the Board and Trustee of the Fund; Director of Keystone Investments; Chairman of the Board and Trustee or Director of all other funds in the Keystone Investments Family of Funds; Director and Chairman of the Board of Hartwell Keystone; Chairman of the Board and Trustee of Anatolia College; Trustee of University Hospital (and Chairman of its Investment Committee); former Chairman of the Board and Chief Executive Officer of Keystone Investments; and former Chief Executive Officer of the Fund.

EDWIN D. CAMPBELL: Trustee of the Fund; Trustee or Director of all other funds in the Keystone Investments Family of Funds; Executive Director, Coalition of Essential Schools, Brown University; Director and former Executive Vice President, National Alliance of Business; former Vice President, Educational Testing Services; and former Dean, School of Business, Adelphi University.

CHARLES F. CHAPIN: Trustee of the Fund; Trustee or Director of all other funds in the Keystone Investments Family of Funds; former Group Vice President, Textron Corp.; and former Director, Peoples Bank (Charlotte, N.C).

LEROY KEITH, JR.: Trustee of the Fund; Trustee or Director of all other funds in the Keystone Investments Family of Funds; Director of Phoenix Total Return Fund and Equifax, Inc.; Trustee of Phoenix Series Fund, Phoenix Multi-Portfolio Fund and The Phoenix Big Edge Series Fund; and former President, Morehouse College.

K. DUN GIFFORD: Trustee of the Fund; Trustee or Director of all other funds in the Keystone Investments Family of Funds; Chairman of the Board, Director and Executive Vice President, The London Harness Company; Managing Partner, Roscommon Capital Corp.; Trustee, Cambridge College; Chairman Emeritus and Director, American Institute of Food and Wine; Chief Executive Officer, Gifford Gifts of Fine Foods; Chairman, Gifford, Drescher & Associates (environmental consulting); President, Oldways Preservation and Exchange Trust (education); and former Director, Keystone Investments and Keystone.

F. RAY KEYSER, JR.: Trustee of the Fund; Trustee or Director of all other funds in the Keystone Investments Family of Funds; Of Counsel, Keyser, Crowley & Meub, P.C.; Member, Governor's (VT) Council of Economic Advisers; Chairman of the Board and Director, Central Vermont Public Service Corporation and Hitchcock Clinic; Director, Vermont Yankee Nuclear Power Corporation, Vermont Electric Power Company, Inc., Grand Trunk Corporation, Central Vermont Railway, Inc., S.K.I. Ltd., Sherburne Corporation, Union Mutual Fire Insurance Company, New England Guaranty Insurance Company, Inc. and the Investment Company Institute; former Governor of Vermont; former Director and President, Associated Industries of Vermont; former Chairman and President, Vermont Marble Company; former Director of Keystone; and former Director and Chairman of the Board, Green Mountain Bank.

DAVID M. RICHARDSON: Trustee of the Fund; Trustee or Director of all other funds in the Keystone Investments Family of Funds; Executive Vice President, DHR International, Inc. (executive recruitment); former Senior Vice President, Boyden International Inc. (executive recruitment); and Director, Commerce and Industry Association of New Jersey, 411 International, Inc. and J & M Cumming Paper Co.

RICHARD J. SHIMA: Trustee of the Fund; Trustee or Director of all other funds in the Keystone Investments Family of Funds; Chairman, Environmental Warranty, Inc., and Consultant, Drake Beam Morin, Inc. (executive outplacement); Director of Connecticut Natural Gas Corporation, Trust Company of Connecticut, Hartford Hospital, Old State House Association and Enhanced Financial Services, Inc.; Member, Georgetown College Board of Advisors; Chairman, Board of Trustees, Hartford Graduate Center; Trustee, Kingswood-Oxford School and Greater Hartford YMCA; former Director, Executive Vice President and Vice Chairman of The Travelers Corporation; and former Managing Director of Russell Miller, Inc.

ANDREW J. SIMONS: Trustee of the Fund; Trustee or Director of all other funds in the Keystone Investments Family of Funds; Partner, Farrell, Fritz, Caemmerer, Cleary, Barnosky & Armentano, P.C.; President, Nassau County Bar Association; former Associate Dean and Professor of Law, St. John's University School of Law.

EDWARD F. GODFREY: Senior Vice President of the Fund; Senior Vice President of all other funds in the Keystone Investments Family of Funds; Director, Senior Vice President, Chief Financial Officer and Treasurer of Keystone Investments, the Principal Underwriter, Keystone Asset Corporation, Keystone Capital Corporation, Keystone Trust Company; Treasurer of Keystone Institutional, Robert Van Partners, Inc., and FICO; Treasurer and Director of Keystone Management, Keystone Software, Inc., and Hartwell Keystone; Vice President and Treasurer of KFIA; and Director of KIRC.

JAMES R. McCALL: Senior Vice President of the Fund; Senior Vice President of all other funds in the Keystone Investments Family of Funds; and President of Keystone.

BETSY A. BLACHER: Vice President of the Fund; Vice President of certain other funds in the Keystone Investments Family of Funds; and Senior Vice President of Keystone.

KEVIN J. MORRISSEY: Treasurer of the Fund; Treasurer of all other funds in the Keystone Investments Family of Funds; Vice President of Keystone Investments; Assistant Treasurer of FICO and Keystone; and former Vice President and Treasurer of KIRC.

ROSEMARY D. VAN ANTWERP: Senior Vice President and Secretary of the Fund; Senior Vice President and Secretary of all other funds in the Keystone Investments Family of Funds; Senior Vice President, General Counsel and Secretary of Keystone; Senior Vice President, General Counsel, Secretary and Director of the Principal Underwriter, Keystone Management and Keystone Software; Senior Vice President and General Counsel of Keystone Institutional; Senior Vice President, General Counsel and Director of FICO and KIRC; Senior Vice President and Secretary of Hartwell Keystone and Robert Van Partners, Inc.; Vice President and Secretary of KFIA; and Senior Vice President, General Counsel and Secretary of Keystone Investments, Keystone Asset Corporation, Keystone Capital Corporation and Keystone Trust Company.

* This Trustee may be considered an "interested person" within the meaning of the 1940 Act.

Mr. Elfner and Mr. Bissell are "interested persons" by virtue of their positions as officers and/or Directors of Keystone Investments and several of its affiliates including Hartwell Keystone, the Principal Underwriter and KIRC. Mr. Elfner and Mr. Bissell own shares of Keystone Investments. Mr. Elfner is Chairman of the Board, Chief Executive Officer and Director of Keystone Investments. Mr. Bissell is a Director of Keystone Investments.

During the fiscal year ended December 31, 1994, none of the affiliated Trustees and officers of the Fund received any direct remuneration from the Fund. During this same period, the nonaffiliated Trustees received $56,308 in retainers and fees. For the year ending December 31, 1994, fees paid to Independent Trustees on a fund complex wide basis were approximately $585,990. On March 31, 1995, the Trustees and officers of the Fund, as a group, beneficially owned less than 1% of the Fund's then outstanding shares.

The address of all the Fund's Trustees and officers is 200 Berkeley Street, Boston, Massachusetts 02116-5034.

DECLARATION OF TRUST

The Fund is a Massachusetts business trust originally established under a Declaration of Trust dated April 12, 1977. On July 27, 1993, the Fund's Declaration of Trust was amended and restated in its entirety (the "Declaration of Trust"). The Fund is similar in most respects to a business corporation. The principal distinction between the Fund and a corporation relates to the shareholder liability described below. This summary is qualified in its entirety by reference to the Declaration of Trust.

SHAREHOLDER LIABILITY

Pursuant to certain decisions of the Supreme Judicial Court of Massachusetts, shareholders of a Massachusetts business trust may, under certain circumstances, be held personally liable as partners for the obligations of the trust. Even if, however, the Fund were held to be a partnership, the possibility of the shareholders incurring financial loss for that reason appears remote because the Fund's Declaration of Trust contains an express disclaimer of shareholder liability for obligations of the Fund and requires that notice of such disclaimer be given in each agreement, obligation or instrument entered into or executed by the Fund or the Trustees, and because the Declaration of Trust provides for indemnification out of the trust property for any shareholder held personally liable for the obligations of the Fund.

VOTING RIGHTS

Under the terms of the Declaration of Trust, shares are entitled to vote in the election of Trustees and on other matters and no amendment may be made to the Declaration of Trust without the approval of the shareholders of the Fund. Shares have non-cumulative voting rights, which means that the holders of more than 50% of the shares voting for the election of Trustees can elect 100% of the Trustees to be elected at a meeting, and, in such event, the holders of the remaining less than 50% of the shares will not be able to elect any Trustees.

LIMITATION OF TRUSTEES' LIABILITY

The Declaration of Trust provides that a Trustee shall be liable only for his own willful defaults and, if reasonable care has been exercised in the selection of officers, agents, employees or investment advisers, shall not be liable for any neglect or wrongdoing of any such person; provided, however, that nothing in the Declaration of Trust shall protect a Trustee against any liability for his willful misfeasance, bad faith, gross negligence or reckless disregard of his duties.

INVESTMENT MANAGER

Subject to the general supervision of the Fund's Board of Trustees, Keystone Management, located at 200 Berkeley Street, Boston, Massachusetts 02116-5034, serves as investment manager to the Fund and is responsible for the overall management of the Fund's business and affairs. Keystone Management, organized in 1989, is a wholly-owned subsidiary of Keystone and its directors and principal executive officers have been affiliated with Keystone, a seasoned investment adviser, for a number of years. Keystone Management also serves as investment manager to each of the funds in the Keystone Fund Family and to certain other funds in the Keystone Investments Family of Funds.

Except as otherwise noted below, pursuant to an Investment Management Agreement with the Fund (the "Management Agreement") and subject to the supervision of the Fund's Board of Trustees, Keystone Management manages and administers the operation of the Fund and manages the investment and reinvestment of the Fund's assets in conformity with the Fund's investment objectives and restrictions. The Management Agreement stipulates that Keystone Management shall provide office space, all necessary office facilities, equipment and personnel in connection with its services under the Management Agreement and pay or reimburse the Fund for the compensation of Fund officers and trustees who are affiliated with the investment manager as well as pay all expenses of Keystone Management incurred in connection with the provision of its services. All charges and expenses other than those specifically referred to as being borne by Keystone Management will be paid by the Fund, including, but not limited to, custodian charges and expenses; bookkeeping and auditors' charges and expenses; transfer agent charges and expenses; fees of Independent Trustees; brokerage commissions, brokers' fees and expenses; issue and transfer taxes; costs and expenses under the Distribution Plan; taxes and trust fees payable to governmental agencies; the cost of share certificates; fees and expenses of the registration and qualification of the Fund and its shares with the Securities and Exchange Commission (sometimes referred to herein as the "SEC" or the "Commission") or under state or other securities laws; expenses of preparing, printing and mailing prospectuses, statements of additional information, notices, reports and proxy materials to shareholders of the Fund; expenses of shareholders' and Trustees' meetings; charges and expenses of legal counsel for the Fund and for the Trustees of the Fund on matters relating to the Fund; charges and expenses of filing annual and other reports with the SEC and other authorities; and all extraordinary charges and expenses of the Fund; provided, however that Keystone Management pays all charges and expenses relating to these items subject to reimbursement by the Fund.

The Management Agreement permits Keystone Management to enter into an agreement with Keystone or another investment adviser, under which Keystone or such other investment adviser, as investment adviser, will provide substantially all the services to be provided by Keystone Management under the Management Agreement. The Management Agreement also permits Keystone Management to delegate to Keystone or another investment adviser substantially all of the investment manager's rights, duties and obligations under the Management Agreement. Keystone Management provides the Fund with certain administrative and management services, which services include (1) performing research and planning with respect to (a) the Fund's qualification as a regulated investment company under Subchapter M of the Internal Revenue Code, (b) tax treatment of the Fund's portfolio investments, (c) tax treatment of special corporate actions (such as reorganizations), (d) state tax matters affecting the Fund, and (e) the Fund's distributions of income and capital gains; (2) preparing the Fund's federal and state tax returns; (3) providing services to the Fund's shareholders in connection with federal and state taxation and distributions of income and capital gains; and (4) storing documents relating to the Fund's activities.

The Fund pays Keystone Management at the end of each calendar month a fee for its services consisting of (1) an amount calculated as set forth below:

ANNUAL MANAGEMENT FEE		INCOME	AGGREGATE NET ASSET VALUE OF THE SHARES OF THE FUND
		2.0% of Gross Dividend and Interest Income Plus	
0.50%	of the first		$100,000,000, plus
0.45%	of the next		$100,000,000, plus
0.40%	of the next		$100,000,000, plus
0.35%	of the next		$100,000,000, plus
0.30%	of the next		$100,000,000, plus
0.25%	of amounts over		$500,000,000; and

(2) an amount equal to Keystone Management's reimbursable expenses accrued during such calendar month.

As a continuing condition of registration of shares in a state, Keystone Management has agreed to reimburse the Fund annually for certain operating expenses incurred by the Fund in excess of certain percentages of the Fund's average daily net assets. However, Keystone Management is not required to make such reimbursements to an extent which would result in the Fund's inability to qualify as a regulated investment company under provisions of the Internal Revenue Code. This condition may be modified or eliminated in the future.

The Management Agreement continues in effect from year to year only if approved at least annually by the Fund's Board of Trustees or by a vote of a majority of the outstanding shares, and such renewal has been approved by the vote of a majority of the Independent Trustees cast in person at a meeting called for the purpose of voting on such approval. The Management Agreement may be terminated, without penalty, by the Fund's Board of Trustees or by a vote of a majority of outstanding shares on 60 days' written notice to Keystone, and by Keystone on 90 days' written notice to the Fund. The Management Agreement will terminate automatically upon its "assignment" as that term is defined in the 1940 Act.

For additional discussion of fees paid to Keystone Management, see "Investment Adviser" below.

INVESTMENT ADVISER

Pursuant to the Management Agreement, Keystone Management has delegated its investment management functions, except for certain administrative and management services, to Keystone and has entered into an Investment Advisory Agreement (the "Advisory Agreement") with Keystone under which Keystone provides investment advisory and management services to the Fund.

Keystone, located at 200 Berkeley Street, Boston, Massachusetts 02116-5034, has provided investment advisory and management services to investment companies and private accounts since it was organized in 1932. Keystone is a wholly-owned subsidiary of Keystone Investments, 200 Berkeley Street, Boston, Massachusetts 02116-5034.

Keystone Investments is a corporation predominantly owned by current and former members of Keystone's management and its affiliates. The shares of Keystone Investments common stock beneficially owned by management are held in a number of voting trusts, the trustees of which are George S. Bissell, Albert H. Elfner, III, Edward F. Godfrey and Ralph J. Spuehler, Jr. Keystone Investments provides accounting, bookkeeping, legal, personnel and general corporate services to Keystone Management, Keystone, their affiliates and the Keystone Investments Family of Funds.

Pursuant to the Advisory Agreement, Keystone receives for its services an annual fee representing 85% of the management fee received by Keystone Management under the Management Agreement.

Under the terms of the Advisory Agreement and subject to the supervision of the Fund's Board of Trustees, Keystone manages and administers the operation of the Fund, and manages the investment and reinvestment of the Fund's assets in conformity with the Fund's investment objective and restrictions. The Advisory Agreement stipulates that Keystone shall provide office space, all necessary office facilities, equipment and personnel in connection with its services under the Advisory Agreement and pay or reimburse the Fund for the compensation of Fund officers and Trustees who are affiliated with the investment manager and pay all expenses of Keystone incurred in connection with the provision of its services. All charges and expenses other than those specifically referred to as being borne by Keystone will ultimately be paid by the Fund, including, but not limited to, custodian charges and expenses; bookkeeping and auditors' charges and expenses; transfer agent charges and expenses; fees of Independent Trustees; brokerage commissions, brokers' fees and expenses; issue and transfer taxes; costs and expenses under the Distribution Plan; taxes and trust fees payable to governmental agencies; the cost of share certificates, fees and expenses of the registration and qualification of the Fund and its shares with the SEC or under state or other securities laws; expenses of preparing, printing and mailing prospectuses, statements of additional information, notices, reports and proxy materials to shareholders of the Fund; expenses of shareholders' and Trustees' meetings; charges and expenses of legal counsel for the Fund and for the Trustees of the Fund on matters relating to the Fund; charges and expenses of filing annual and other reports with the SEC and other authorities; and all extraordinary charges and expenses of the Fund.

During the fiscal year ended December 31, 1992, the Fund paid or accrued to Keystone Management investment management fees of $5,483,861, which represented 0.46% of the Fund's average net assets. Of such amount paid to Keystone Management, $4,661,282 was paid to Keystone for its services to the Fund. In addition, the Fund reimbursed Keystone Management $1,570,163, which represented 0.13% of the Fund's average net assets, in connection with reimbursable expenses paid by Keystone Management on behalf of the Fund. For the fiscal year ended December 31, 1992, the total fee paid to Keystone Management by the Fund for investment management and administrative services fees was $7,054,024, which represented 0.59% of the Fund's average net assets.

During the fiscal year ended December 31, 1993, the Fund paid or accrued to Keystone Management investment management fees of $6,507,055, which represented 0.43% of the Fund's average net assets. Of such amount paid to Keystone Management, $5,530,997 was paid to Keystone for its services to the Fund. In addition, the Fund reimbursed Keystone Management $2,488,890, which represented 0.16% of the Fund's average net assets, in connection with reimbursable expenses paid by Keystone Management on behalf of the Fund. For the fiscal year ended December 31, 1993, the total fee paid to Keystone Management by the Fund for investment management and administrative services fees was $8,995,945, which represented 0.59% of the Fund's average net assets.

During the fiscal year ended December 31, 1994, the Fund paid or accrued to Keystone Management investment management fees of $5,941,545 which represented 0.43% of the Fund's average net assets. Of such amount paid to Keystone Management, $5,050,313 was paid to Keystone for its services to the Fund. In addition, the Fund reimbursed Keystone Management $2,029,000, which represented 0.15% of the Fund's average net assets, in connection with reimbursable expenses paid by Keystone Management on behalf of the Fund. For the fiscal year ended December 31, 1994, the total fee paid to Keystone Management by the Fund for investment management and administrative services fees was $7,970,545, which represented 0.58% of the Fund's average net assets.

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BROKERAGE

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It is the policy of the Fund, in effecting transactions in portfolio securities, to seek best execution of orders at the most favorable prices. The determination of what may constitute best execution and price in the execution of a securities transaction by a broker involves a number of considerations, including, without limitation, the overall direct net economic result to the Fund, involving both price paid or received and any commissions and other costs paid, the efficiency with which the transaction is effected, the ability to effect the transaction at all where a large block is involved, the availability of the broker to stand ready to execute potentially difficult transactions in the future and the financial strength and stability of the broker. Such considerations are judgmental and are weighed by management in determining the overall reasonableness of brokerage commissions paid.

Subject to the foregoing, a factor in the selection of brokers is the receipt of research services, such as analyses and reports concerning issuers, industries, securities, economic factors and trends and other statistical and factual information. Any such research and other statistical and factual information provided by brokers to the Fund, Keystone Management or Keystone is considered to be in addition to and not in lieu of services required to be performed by Keystone Management under the Management Agreement or Keystone under the Advisory Agreement. The cost, value and specific application of such information are indeterminable and cannot be practically allocated among the Fund and other clients of Keystone Management or Keystone who may indirectly benefit from the availability of such information. Similarly, the Fund may indirectly benefit from information made available as a result of transactions effected for such other clients. Under the Management Agreement and the Advisory Agreement, Keystone Management and Keystone are permitted to pay higher brokerage commissions for brokerage and research services in accordance with Section 28(e) of the Securities Exchange Act of 1934. In the event Keystone Management and Keystone do follow such a practice, they will do so on a basis that is fair and equitable to the Fund.

The Fund's securities transactions are generally principal transactions with the issuer of the security or with major underwriters and dealers for municipal bonds. Accordingly, the Fund does not pay significant brokerage commissions. The cost of securities purchased from underwriters includes an underwriting commission or concession and the prices at which securities are purchased from and sold to dealers include a dealer's mark-up or mark-down. Purchases from underwriters will include the underwriting commission or concession and purchases from dealers serving as market makers will include the spread between the bid and asked prices. Where transactions are made in the over-the-counter market, the Fund will deal with primary market makers unless more favorable prices are otherwise obtainable.

The Fund may participate, if and when practicable, in group bidding for the purchase directly from an issuer of certain securities for the Fund's portfolio in order to take advantage of the lower purchase price available to members of such a group.

Neither Keystone Management, Keystone nor the Fund intend to place securities transactions with any particular broker-dealer or group thereof. However, the Fund's Board of Trustees has determined that the Fund may follow a policy of considering sales of shares as a factor in the selection of broker-dealers to execute portfolio transactions, subject to the requirements of best execution, including best price, described above.

The policy of the Fund with respect to brokerage is and will be reviewed by the Fund's Board of Trustees from time to time. Because of the possibility of further regulatory developments affecting the securities exchanges and brokerage practices generally, the foregoing practices may be changed, modified or eliminated.

Investment decisions for the Fund are made independently by Keystone Management or Keystone from those of the other funds and investment accounts managed by Keystone Management or Keystone. It may frequently develop that the same investment decision is made for more than one fund. Simultaneous transactions are inevitable when the same security is suitable for the investment objective of more than one account. When two or more funds or accounts are engaged in the purchase or sale of the same security, the transactions are allocated as to amount in accordance with a formula that is equitable to each fund or account. It is recognized that in some cases this system could have a detrimental effect on the price or volume of the security as far as the Fund is concerned. In other cases, however, it is believed that the ability of the Fund to participate in volume transactions will produce better executions for the Fund.

For the fiscal years ended December 31, 1992, 1993 and 1994, the Fund did not pay any brokerage commissions for securities transactions.

In no instance are portfolio securities purchased from or sold to Keystone Management, Keystone, the Principal Underwriter or any of their affiliated persons, as defined in the 1940 Act and rules and regulations issued thereunder.

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STANDARDIZED TOTAL RETURN AND YIELD QUOTATIONS

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Total return quotations for the Fund as they may appear from time to time in advertisements are calculated by finding the average annual compounded rates of return over the one, five and ten year periods on a hypothetical $1,000 investment that would equate the initial amount invested to the ending redeemable value. To the initial investment all dividends and distributions are added, and all recurring fees charged to all shareholder accounts are deducted. The ending redeemable value assumes a complete redemption at the end of the one, five or ten year periods.

The cumulative total returns of the Fund for the one, five and ten years ended December 31, 1994 were (9.96)% (including contingent deferred sales charge), 30.92% and 124.42%, respectively. The average annual total returns for the one, five and ten year periods ended December 31, 1994 were (9.96)%, 5.54% and 8.42%, respectively.

Current yield quotations as they may appear from time to time in advertisements will consist of a quotation based on a 30-day period ended on the date of the most recent balance sheet of the Fund, computed by dividing the net investment income per share earned during the period by the maximum offering price per share on the last day of the base period. The current yield for the 30-day period ended December 31, 1994 was 5.59%.

Tax equivalent yield is, in general, the current yield divided by a factor equal to one minus a stated income tax rate and reflects the yield a taxable investment would have to achieve in order to equal on an after tax-basis a tax exempt yield. The tax equivalent yield for an investor in the 31% federal tax bracket for the 30-day period ended December 31, 1994 was 8.10%.

Any given yield or total return quotation should not be considered representative of the Fund's yield or total return for any future period.

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ADDITIONAL INFORMATION

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State Street Bank and Trust Company, 225 Franklin Street, Boston, Massachusetts 02110, is the custodian ("Custodian") of all securities and cash of the Fund. The Custodian performs no investment management functions for the Fund, but, in addition to its custodial services, is responsible for accounting and related recordkeeping on behalf of the Fund.

KPMG Peat Marwick LLP, One Boston Place, Boston, Massachusetts 02108, Certified Public Accountants, are the independent auditors for the Fund.

KIRC, located at 101 Main Street, Cambridge, Massachusetts 02142, is a wholly-owned subsidiary of Keystone, and acts as transfer agent and dividend disbursing agent for the Fund.

Except as otherwise stated in its prospectus or required by law, the Fund reserves the right to change the terms of the offer stated in its prospectus without shareholder approval, including the right to impose or change fees for services provided.

No dealer, salesman or other person is authorized to give any information or to make any representation not contained in the Fund's prospectus, this statement of additional information, or in supplemental sales literature issued by the Fund or the Principal Underwriter, and no person is entitled to rely on any information or representation not contained therein.

The Fund's prospectus and this statement of additional information omit certain information contained in the registration statement filed with the Securities and Exchange Commission, which may be obtained from the Commission's principal office in Washington, D.C. upon payment of the fee prescribed by the rules and regulations promulgated by the Commission.

As of March 31, 1995, Merrill Lynch Pierce Fenner & Smith, Attn: Book Entry, 4800 Deer Lake Dr. E., 3rd Floor, Jacksonville, FL 32246-6484 owned of record 18.3% of the Fund's outstanding shares.

APPENDIX

MUNICIPAL BONDS

Municipal bonds include debt obligations issued by or on behalf of a state, a territory, or a possession of the United States, the District of Columbia or any political subdivision, agency or instrumentality thereof (for example, counties, cities, towns, villages, districts, authorities) to obtain funds for various public purposes, including the construction of a wide range of public facilities such as airports, bridges, highways, housing, hospitals, mass transportation, schools, streets and water and sewer works. Other public purposes for which municipal bonds may be issued include the refunding of outstanding obligations, obtaining funds for general operating expenses and obtaining funds to lend to public or private institutions for the construction of facilities such as educational, hospital and housing facilities. In addition, certain types of industrial development bonds have been or may be issued by or on behalf of public authorities to finance certain privately operated facilities and certain local facilities for water supply, gas, electricity or sewage or solid waste disposal. Such obligations are included within the term municipal bonds if the interest paid thereon qualifies as exempt from federal income tax. The income of certain types of industrial development bonds used to finance certain privately operated facilities (qualified "private activity" bonds) issued after August 7, 1986, while exempt from federal income tax, is includable for purposes of the calculation of the alterative minimum tax. Other types of industrial development bonds, the proceeds of which are used for the construction, equipment, repair or improvement of privately operated industrial or commercial facilities, may constitute municipal bonds, although the current federal tax laws place substantial limitations on the size of such issues.

The two principal classifications of municipal bonds are "general obligation" and "limited obligation" or "revenue" bonds. General obligation bonds are obligations involving the credit of an issuer possessing taxing power and are payable from the issuer's general unrestricted revenues and not from any particular fund or revenue source. Their payment may be dependent upon an appropriation by the issuer's legislative body and may be subject to quantitative limitations on the issuer's taxing power. The characteristics and methods of enforcement of general obligation bonds vary according to the law applicable to the particular issuer. Limited obligation or revenue bonds are payable only from the revenues derived from a particular facility or class of facilities or, in some cases, from the proceeds of a special excise or other specific revenue source, such as the user of the facility. Industrial development bonds that are municipal bonds are in most cases revenue bonds and generally are not payable from the unrestricted revenues of the issuer. The credit quality of industrial development revenue bonds is usually directly related to the credit standing of the owner or user of the facilities. There are, of course, variations in the security of municipal bonds, both within a particular classification and between classifications, depending on numerous factors.

The yields on municipal bonds are dependent on a variety of factors, including general money market conditions, the financial condition of the issuer, general conditions of the municipal bond market, size of a particular offering, the maturity of the obligation and rating of the issue. The ratings of Moody's Investors Service, Inc. ("Moody's"), Standard & Poor's Corporation ("S&P") and Fitch Investor Services, Inc. ("Fitch"), as described herein and in the prospectus, represent their opinions as to the quality of the municipal bonds that they undertake to rate. It should be emphasized, however, that ratings are general and are not absolute standards of quality. Consequently, municipal bonds with the same maturity, interest rate and rating may have different yields while municipal bonds of the same maturity and interest rate with different ratings may have the same yield. It should also be noted that the standards of disclosure applicable to and the amount of information relating to the financial condition of issuers of municipal bonds are not as extensive as those generally relating to corporations.

Subsequent to its purchase by the Fund, an issue of municipal bonds or other investment may cease to be rated or its rating may be reduced below the minimum rating required for purchase by the Fund. Neither event requires the elimination of such obligation from the Fund's portfolio, but Keystone will consider such an event in its determination of whether the Fund should continue to hold such obligation in its portfolio.

The ability of the Fund to achieve its investment objective is dependent upon the continuing ability of issuers of municipal bonds to meet their obligations to pay interest and principal when due. Obligations of issuers of municipal bonds, including municipal bonds issued by them, are subject to the provisions of bankruptcy, insolvency and other laws affecting the rights and remedies of creditors, such as the federal Bankruptcy Act, and laws, if any, that may be enacted by Congress or state legislatures extending the time for payment of principal or interest, or both, or imposing other constraints upon enforcement of such obligations. There is also the possibility that as a result of litigation or other conditions, the power or ability of any one or more issuers to pay, when due, principal of and interest on its or their municipal bonds may be materially affected. In addition the market for municipal bonds is often thin and can be temporarily affected by large purchases and sales including those by the Fund.

From time to time, proposals have been introduced before Congress for the purpose of restricting or eliminating the federal income tax exemption for interest on municipal bonds, and similar proposals may well be introduced in the future. If such a proposal were enacted, the availability of municipal bonds for investment by the Fund and the value of the Fund's portfolio could be materially affected; in which event, the Fund would reevaluate its investment objective and policies and consider changes in the structure of the Fund or dissolution.

DESCRIPTION OF BOND RATINGS

The Tax Reform Act of 1986 made significant changes in the federal tax status of certain obligations that were previously fully federally tax exempt. As a result, three categories of such obligations issued after August 7, 1986 now exist: (1) "public purpose" bonds, the income of which remains fully exempt from federal income tax; (2) qualified "private activity" industrial development bonds, the income of which, while exempt from federal income tax under Section 103 of the Internal Revenue Code, as amended (the "Code") is includable in the calculation of the federal alternative minimum tax; and (3) "private activity" (private purpose) bonds, the income of which is not exempt from federal income tax. The Fund will not invest in private activity (private purpose) bonds, and, except as described under "Other Eligible Securities," will not invest in qualified "private activity" industrial development bonds.

CORPORATE AND MUNICIPAL BOND RATINGS

S&P CORPORATE AND MUNICIPAL BOND RATINGS

A. MUNICIPAL NOTES

An S&P note rating reflects the liquidity concerns and market access risks unique to notes. Notes due in 3 years or less will likely receive a note rating. Notes maturing beyond 3 years will most likely receive a long term debt rating. The following criteria are used in making that assessment:

a. Amortization schedule (the larger the final maturity relative to other maturities the more likely it will be treated as a note); and

b. Source of payment (the more dependent the issue is on the market for its refinancing, the more likely it will be treated as a note).

Note ratings are as follows:

1. SP-1 Very strong or strong capacity to pay principal and interest. Those issues determined to possess overwhelming safety characteristics will be given a plus (+) designation.

2. SP-2 Satisfactory capacity to pay principal and interest.

3. SP-3 Speculative capacity to pay principal and interest.

B. TAX EXEMPT DEMAND BONDS

S&P assigns "dual" ratings to all long-term debt issues that have as part of their provisions a demand or double feature.

The first rating addresses the likelihood of repayment of principal and interest as due, and the second rating addresses only the demand feature. The long-term debt rating symbols are used for bonds to denote the long-term maturity and the commercial paper rating symbols are used to denote the put option (for example, "AAA/A-1+"). For the newer "demand notes," S&P note rating symbols, combined with the commercial paper symbols, are used (for example, "SP-1+/A-1+").

C. CORPORATE AND MUNICIPAL BOND RATINGS

An S&P corporate or municipal bond rating is a current assessment of the creditworthiness of an obligor, including obligors outside the U.S., with respect to a specific obligation. This assessment may take into consideration obligors such as guarantors, insurers, or lessees. Ratings of foreign obligors do not take into account currency exchange and related uncertainties. The ratings are based on current information furnished by the issuer or obtained by S&P from other sources it considers reliable.

The ratings are based, in varying degrees, on the following considerations:

a. Likelihood of default - capacity and willingness of the obligor as to the timely payment of interest and repayment of principal in accordance with the terms of the obligation;

b. Nature of and provisions of the obligation; and

c. Protection afforded by and relative position of the obligation in the event of bankruptcy reorganization or other arrangement under the laws of bankruptcy and other laws affecting creditors' rights.

PLUS (+) OR MINUS (-): To provide more detailed indications of credit quality, ratings from "AA" TO "BBB" may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories.

A provisional rating is sometimes used by S&P. It assumes the successful completion of the project being financed by the debt being rated and indicates that payment of debt service requirements is largely or entirely dependent upon the successful and timely completion of the project. This rating, however, while addressing credit quality subsequent to completion of the project, makes no comment on the likelihood of, or the risk of default upon failure of, such completion.

Bond ratings are as follows:

1. AAA - Debt rated AAA has the highest rating assigned by S&P. Capacity to pay interest and repay principal is extremely strong.

2. AA - Debt rated AA has a very strong capacity to pay interest and repay principal and differs from the higher rated issues only in small degree.

3. A - Debt rated A has a strong capacity to pay interest and repay principal although it is somewhat more susceptible to the adverse effects of changes in circumstances and economic conditions than debt in higher rated categories.

4. BBB - Debt rated BBB is regarded as having an adequate capacity to pay interest and repay principal. Whereas it normally exhibits adequate protection parameters, adverse economic conditions or changing circumstances are more likely to lead to a weakened capacity to pay interest and repay principal for debt in this category than in higher rated categories.

MOODY'S CORPORATE AND MUNICIPAL BOND RATINGS

Moody's ratings are as follows:

1. Aaa - Bonds that are rated Aaa are judged to be of the best quality. They carry the smallest degree of investment risk and are generally referred to as "gilt-edge." Interest payments are protected by a large or by an exceptionally stable margin and principal is secure. While the various protective elements are likely to change, such changes as can be visualized are most unlikely to impair the fundamentally strong position of such issues.

2. Aa - Bonds that are rated Aa are judged to be of high quality by all standards. Together with the Aaa group they comprise what are generally known as high grade bonds. They are rated lower than the best bonds because margins of protection may not be as large as in Aaa securities or fluctuation of protective elements may be of greater amplitude or there may be other elements present that make the long-term risks appear somewhat larger than in Aaa securities.

3. A - Bonds that are rated A possess many favorable investment attributes and are to be considered as upper medium grade obligations. Factors giving security to principal and interest are considered adequate but elements may be present that suggest a susceptibility to impairment sometime in the future.

4. Baa - Bonds that are rated Baa are considered as medium grade obligations, i.e., they are neither highly protected nor poorly secured. Interest payments and principal security appear adequate for the present but certain protective elements may be lacking or may be characteristically unreliable over any great length of time. Such bonds lack outstanding investment characteristics and in fact have speculative characteristics as well.

Moody's applies numerical modifiers, 1, 2 and 3 in each generic rating classification from Aa through Baa in its corporate bond rating system. The modifier 1 indicates that the security ranks in the higher end of its generic rating category; the modifier 2 indicates a mid-range ranking; and the modifier 3 indicates that the issue ranks in the lower end of its generic rating category.

Con. (---) - Municipal bonds for which the security depends upon the completion of some act or the fulfillment of some condition are rated conditionally. These are bonds secured by (a) earnings of projects under construction, (b) earnings of projects unseasoned in operation experience, (c) rentals that begin when facilities are completed, or (d) payments to which some other limiting condition attaches. Parenthetical rating denotes probable credit stature upon completion of construction or elimination of basis of condition.

Those municipal bonds in the Aa, A, and Baa groups that Moody's believes possess the strongest investment attributes are designated by the symbols Aa 1, A 1, and Baa 1.

MONEY MARKET INSTRUMENTS

The Fund's investments in commercial paper are limited to those rated A-1 by S&P, Prime-1 by Moody's, or F-1 by Fitch. These ratings and other money market instruments are described as follows:

COMMERCIAL PAPER RATINGS

Commercial paper rated A-1 by S&P has the following characteristics. Liquidity ratios are adequate to meet cash requirements. The issuer's long-term senior debt is rated "A" or better, although in some cases "BBB" credits may be allowed. The issuer has access to at least two additional channels of borrowing. Basic earnings and cash flow have an upward trend with allowance made for unusual circumstances. Typically, the issuer's industry is well established and the issuer has a strong position within the industry.

Commercial paper rated A-2 by S&P has the same characteristics as that rated A-1 except that the relative degree of safety is not as overwhelming.

Commercial paper rated A-3 has a satisfactory capacity for timely payment. However, it is somewhat more vulnerable to the adverse effects of changes in circumstances than obligations rated A-1 or A-2.

The rating Prime-1 is the highest commercial paper rating assigned by Moody's. Among the factors considered by Moody's in assigning ratings are the following: (1) evaluation of the management of the issuer; (2) economic evaluation of the issuer's industry or industries and an appraisal of speculative-type risks which may be inherent in certain areas; (3) evaluation of the issuer's products in relation to competition and customer acceptance; (4) liquidity; (5) amount and quality of long-term debt; (6) trend of earnings over a period of ten years; (7) financial strength of a parent company and the relationships that exist with the issuer; and (8) recognition by the management of obligations that may be present or may arise as a result of public preparations to meet such obligations. Relative strength or weakness of the above factors determines how the issuer's commercial paper is rated within various categories.

Commercial paper rated Prime-2 by Moody's is considered somewhat lower than the best commercial paper because margins of protection may not be as large or because fluctuations of protective elements over the near or intermediate term may be of greater amplitude.

UNITED STATES GOVERNMENT SECURITIES

Securities issued or guaranteed by the U.S. Government include a variety of Treasury securities that differ only in their interest rates, maturities and dates of issuance. Treasury bills have maturities of one year or less. Treasury notes have maturities of one to ten years and Treasury bonds generally have maturities of greater than ten years at the date of issuance.

Securities issued or guaranteed by the U.S. Government or its agencies or instrumentalities include direct obligations of the United States Treasury and securities issued or guaranteed by the Federal Housing Administration, Farmers Home Administration, Export-Import Bank of the United States, Small Business Administration, Government National Mortgage Association, General Services Administration, Central Bank for Cooperatives, Federal Home Loan Banks, Federal Loan Mortgage Corporation, Federal Intermediate Credit Banks, Federal Land Banks, Maritime Administration, The Tennessee Valley Authority, District of Columbia Armory Board and Federal National Mortgage Association.

Some obligations of U.S. Government agencies and instrumentalities, such as Treasury bills and Government National Mortgage Association ("GNMA") pass-through certificates, are supported by the full faith and credit of the United States; others, such as securities of Federal Home Loan Banks, by the right of the issuer to borrow from the Treasury; still others, such as bonds issued by the Federal National Mortgage Association, a private corporation, are supported only by the credit of the instrumentality. Because the U.S. Government is not obligated by law to provide support to an instrumentality it sponsors, the Fund will invest in the securities issued by such an instrumentality only when Keystone determines that the credit risk with respect to the instrumentality does not make its securities unsuitable investments. U.S. Government securities will not include international agencies or instrumentalities in which the U.S. Government, its agencies or instrumentalities participate, such as the International Bank for Reconstruction and Development (the "World Bank"), the Asian Development Bank or the Inter-American Development Bank, or issues insured by the Federal Deposit Insurance Corporation.

CERTIFICATES OF DEPOSITS

Certificates of deposit are receipts issued by a bank in exchange for the deposit of funds. The issuer agrees to pay the amount deposited plus interest to the bearer of the receipt on the date specified on the certificate. The certificate usually can be traded in the secondary market prior to maturity.

Certificates of deposit will be limited to U.S. dollar-denominated certificates of U.S. banks (including their branches abroad) and of U.S. branches of foreign banks that are members of the Federal Reserve System or the Federal Deposit Insurance Corporation, and have at least $1 billion in deposits as of the date of their most recently published financial statements.

The Fund will not acquire time deposits or obligations issued by the World Bank, the Asian Development Bank or the Inter-American Development Bank. Additionally, the Fund does not currently intend to purchase foreign securities (except to the extent that certificates of deposit of foreign branches of U.S. banks may be deemed foreign securities) or purchase certificates of deposit, bankers' acceptances or other similar obligations issued by foreign banks.

BANKERS' ACCEPTANCES

Bankers' acceptances typically arise from short-term credit arrangements designed to enable businesses to obtain funds to finance commercial transactions. Generally, an acceptance is a time draft drawn on a bank by an exporter or an importer to obtain a stated amount of funds to pay for specific merchandise. The draft is then "accepted" by the bank that, in effect, unconditionally guarantees to pay the face value of the instrument on its maturity date. The acceptance may then be held by the accepting bank as an earning asset or it may be sold in the secondary market at the going rate of discount for a specific maturity. Although maturities for acceptances can be as long as 270 days, most acceptances have maturities of six months or less. Bankers' acceptances acquired by the Fund must have been accepted by U.S. commercial banks, including foreign branches of U.S. commercial banks, having total deposits at the time of purchase in excess of $1 billion and must be payable in U.S. dollars.

OPTIONS TRANSACTIONS

The Fund may enter into options transactions. Any premium paid by the Fund in connection with an option transaction may be forfeited if the option expires unexercised.

WRITING COVERED OPTIONS. The Fund writes only covered options. Options written by the Fund will normally have expiration dates of not more than nine months from the date written. The exercise price of the options may be below, equal to, or above the current market values of the underlying securities at the times the options are written.

Unless the option has been exercised, the Fund may close out an option it has written by effecting a closing purchase transaction, whereby it purchases an option covering the same underlying security and having the same exercise price and expiration date (of the same series) as the one it has written. If the Fund desires to sell a particular security on which it has written a call option, it will effect a closing purchase transaction prior to or concurrently with the sale of the security. If the Fund is able to enter into a closing purchase transaction, the Fund will realize a profit (or loss) from such transaction if the cost of such transaction is less (or more) than the premium received from the writing of the option.

An option position may be closed out only in a secondary market for an option of the same series. Although the Fund will generally write only those options for which there appears to be an active secondary market, there is no assurance that a liquid secondary market will exist for any particular option at any particular time, and for some options no secondary market may exist. In such event it might not be possible to effect a closing purchase transaction in a particular option. If the Fund as a covered call option writer is unable to effect a closing purchase transaction, it will not be able to sell the underlying securities until the option expires or it delivers the underlying securities upon exercise.

Because the Fund intends to qualify as a regulated investment company under the Code, the extent to which the Fund may write covered call options and enter into so-called "straddle" transactions involving put and call options may be limited.

Many options are traded on registered securities exchanges. Options traded on such exchanges are issued by the Options Clearing Corporation ("OCC"), a clearing corporation that assumes responsibility for the completion of options transactions.

PURCHASING PUT AND CALL OPTIONS. The Fund can close out a put option it has purchased by effecting a closing sale transaction; for example, the Fund may close out a put option it has purchased by selling a put option. If, however, a secondary market does not exist at a time the Fund wishes to effect a closing sale transaction, the Fund will have to exercise the option to realize any profit. In addition, in a transaction in which the Fund does not own the security underlying a put option it has purchased, the Fund would be required, in the absence of a secondary market, to purchase the underlying security before it could exercise the option. In each such instance, the Fund would incur additional transaction costs.

The Fund may purchase call options for the purpose of offsetting previously written call options of the same series. The Fund also may purchase call options to fix the interest rates of obligations held by it.

The Fund will not purchase a put option if, as a result of such purchase, more than 10% of its total assets would be invested in premiums for such options. The Fund's ability to purchase put and call options may be limited by the Code's requirements for qualification as a regulated investment company.

OPTION WRITING AND RELATED RISKS

The Fund may write covered call and put options. A call option gives the purchaser of the option the right to buy, and the writer the obligation to sell, the underlying security at the exercise price during the option period. Conversely, a put option gives the purchaser the right to sell, and the writer the obligation to buy, the underlying security at the exercise price during the option period.

So long as the obligation of the writer continues, the writer may be assigned an exercise notice by the broker-dealer through whom the option was sold. The exercise notice would require the writer to deliver, in the case of a call, or take delivery of, in the case of a put, the underlying security against payment of the exercise price. This obligation terminates upon expiration of the option, or at such earlier time as the writer effects a closing purchase transaction by purchasing an option of the same series as the one previously sold. Once an option has been exercised, the writer may not execute a closing purchase transaction. For options traded on national securities exchanges ("Exchanges"), to secure the obligation to deliver the underlying security in the case of a call option, the writer of the option is required to deposit in escrow the underlying security or other assets in accordance with the rules of the OCC, an institution created to interpose itself between buyers and sellers of options. Technically, the OCC assumes the order side of every purchase and sale transaction on an Exchange and, by doing so, gives its guarantee to the transaction.

The principal reason for writing options on a securities portfolio is to attempt to realize, through the receipt of premiums, a greater return than would be realized on the underlying securities alone. In return for the premium, the covered call option writer has given up the opportunity for profit from a price increase in the underlying security above the exercise price so long as the option remains open, but retains the risk of loss should the price of the security decline. Conversely, the put option writer gains a profit, in the form of a premium, so long as the price of the underlying security remains above the exercise price, but must purchase the underlying security from the buyer of the put option at the exercise price, even though the price of the security may fall below the exercise price, at any time during the option period. If an option expires, the writer realizes a gain in the amount of the premium. Such a gain may, in the case of a covered call option, be offset by a decline in the market value of the underlying security during the option period. If a call option is exercised, the writer realizes a gain or loss from the sale of the underlying security. If a put option is exercised, the writer must fulfill his obligation to purchase the underlying security at the exercise price, which will usually exceed the then market value of the underlying security. In addition, the premium paid for the put effectively increases the cost of the underlying security, thus reducing the yield otherwise available from such securities.

Because the Fund can write only covered options, it may at times be unable to write additional options unless it sells a portion of its portfolio holdings to obtain new securities against which it can write options. This may result in higher portfolio turnover and correspondingly greater brokerage commissions and other transaction costs.

To the extent that a secondary market is available, the covered option writer may close out options it has written prior to the assignment of an exercise notice by purchasing, in a closing purchase transaction, an option of the same series as the option previously written. If the cost of such a closing purchase plus transaction costs is greater than the premium received upon writing the original option, the writer will incur a loss in the transaction.

OPTIONS TRADING MARKETS

Options that the Fund will trade are generally listed on national securities exchanges. Exchanges on which such options currently are traded are the Chicago Board Options Exchange and the New York, American, Pacific, and Philadelphia Stock Exchanges. Options on some securities may not be listed on any Exchange but traded in the over-the-counter market. Options traded in the over-the-counter market involve the additional risk that securities dealers participating in such transactions would fail to meet their obligations to the Fund. The use of options traded in the over-the-counter market may be subject to limitations imposed by certain state securities authorities. In addition to the limits on its use of options discussed herein, the Fund is subject to the investment restrictions described in the prospectus and statement of additional information.

The staff of the Securities and Exchange Commission ("Commission") currently is of the view that the premiums that the Fund pays for the purchase of unlisted options, and the value of securities used to cover unlisted options written by the Fund, are considered to be invested in illiquid securities or assets for the purpose of calculating whether the Fund is in compliance with its investment restrictions pertaining to illiquid assets and securities.

SPECIAL CONSIDERATIONS APPLICABLE TO OPTIONS

ON TREASURY BONDS AND NOTES. Because trading interest in U.S. Treasury bonds and notes tends to center on most recently auctioned issues, new series of options with expirations to replace expiring options on particular issues will not be introduced indefinitely. Instead, the expirations introduced at the commencement of options trading on a particular issue will be allowed to run their course, with the possible addition of a limited number of new expirations as the original ones expire. Options trading on each series of bonds or notes will thus be phased out as new options are listed on the more recent issues, and a full range of expiration dates will not ordinarily be available for every series on which options are traded.

ON TREASURY BILLS. Because the deliverable U.S. Treasury bill changes from week to week, writers of U.S. Treasury bills call options cannot provide in advance for their potential exercise settlement obligations by acquiring and holding the underlying security. However, if the Fund holds a long position in U.S. Treasury bills with a principal amount corresponding to the option contract size, the Fund may be hedged from a risk standpoint. In addition, the Fund will maintain in a segregated account with its custodian able in the event of an assignment of an exercise notice to ensure that it can meet its open option obligations.

ON GNMA CERTIFICATES. Options on GNMA certificates are not currently traded on any Exchange. However, the Fund may purchase and write such options in the over the counter market, or should they commence trading, on any Exchange.

Since the remaining principal balance of GNMA certificates declines each month as a result of mortgage payments, the Fund, as a writer of a covered GNMA call holding GNMA certificates as "cover" to satisfy its delivery obligation in the event of assignment of an exercise notice, may find that its GNMA certificates no longer have a sufficient remaining principal balance for this purpose. Should this occur, the Fund will enter into a closing purchase transaction or will purchase additional GNMA certificates from the same pool (if obtainable) or replacement GNMA certificates in the cash market in order to remain covered.

A GNMA certificate held by the Fund to cover an option position in any but the nearest expiration month may cease to present cover for the option in the event of a decline in the GNMA coupon rate at which new pools are originated under the FHA/VA loan ceiling in effect at any given time. Should this occur, the Fund will no longer be covered, and the Fund will either enter into a closing purchase transaction or replace the GNMA certificate with a certificate which represents cover. When the Fund closes its position or replaces the GNMA certificate, it may realize an unanticipated loss and incur transaction costs.

RISKS PERTAINING TO THE SECONDARY MARKET. An option position may be closed out only in a secondary market for an option of the same series. Although the Fund will generally purchase or write only those options for which there appears to be an active secondary market, there is no assurance that a liquid secondary market will exist for any particular option at any particular time, and for some options no secondary market may exist. In such event, it might not be possible to effect closing transactions in particular options, with the result that the Fund would have to exercise its options in order to realize any profit and might incur transaction costs in connection therewith. If the Fund as a covered call option writer is unable to effect a closing purchase transaction in a secondary market, it will not be able to sell the underlying security until the option expires or it delivers the underlying security upon exercise.

Reasons for the absence of a liquid secondary market include the following: (i) insufficient trading interest in certain options; (ii) restrictions imposed on transactions; (iii) trading halts, suspensions or other restrictions imposed with respect to particular classes or series of options or underlying securities; (iv) interruption of the normal operations on an Exchange or by a broker; (v) inadequacy of the facilities of an Exchange, the OCC or a broker to handle current trading volume; or (vi) a decision by one or more Exchanges or a broker to discontinue the trading of options (or a particular class or series of options), in which event the secondary market in that class or series of options would cease to exist, although outstanding options that had been issued as a result of trades would generally continue to be exercisable in accordance with their terms.

The hours of trading for options on U.S. government securities may not conform to the hours during which the underlying securities are traded. To the extent that the option markets close before the markets for the underlying securities, significant price and rate movements can take place in the underlying markets that cannot be reflected in the option markets.

FUTURES CONTRACTS AND RELATED OPTIONS TRANSACTIONS

The Fund intends to enter into currency and other financial futures contracts as a hedge against changes in prevailing levels of interest or currency exchange rates to seek relative stability of principal and to establish more definitely the effective return on securities held or intended to be acquired by the Fund or as a hedge against changes in the prices of securities or currencies held by the Fund or to be acquired by the Fund. The Fund's hedging may include sales of futures as an offset against the effect of expected increases in interest or currency exchange rates or securities prices and purchases of futures as an offset against the effect of expected declines in interest or currency exchange rates.

For example, when a fund anticipates a significant market or market sector advance, it will purchase a stock index futures contract as a hedge against not participating in such advance at a time when a fund is not fully invested. The purchase of a futures contract serves as a temporary substitute for the purchase of individual securities, which may then be purchased in an orderly fashion. As such purchases are made, an equivalent amount of index based futures contracts would be terminated by offsetting sales. In contrast, a fund would sell stock index futures contracts in anticipation of or in a general market or market sector decline that may adversely affect the market value of a fund's portfolio. To the extent that the Fund's portfolio changes in value in correlation with a given index, the sale of futures contracts on that index would substantially reduce the risk to the portfolio of a market decline or change in interest rates, and, by so doing, provide an alternative to the liquidation of the Fund's securities positions and the resulting transaction costs.

The Fund intends to engage in options transactions that are related to commodity futures contracts for hedging purposes and in connection with the hedging strategies described above.

Although techniques other than sales and purchases of futures contracts and related options transactions could be used to reduce the Fund's exposure to interest rate and/or market fluctuations, the Fund may be able to hedge its exposure more effectively and perhaps at a lower cost through using futures contracts and related options transactions. The Fund does not intend to take delivery of the instruments underlying futures contracts it holds and does not intend to engage in such futures contracts for speculation.

FUTURES CONTRACTS

Futures contracts are transactions in the commodities markets rather than in the securities markets. A futures contract creates an obligation by the seller to deliver to the buyer the commodity specified in the contract at a specified future time for a specified price. The futures contract creates an obligation by the buyer to accept delivery from the seller of the commodity specified at the specified future time for the specified price. In contrast, a spot transaction creates an immediate obligation for the seller to deliver and the buyer to accept delivery of and pay for an identified commodity. In general, futures contracts involve transactions in fungible goods, such as wheat, coffee and soybeans. However, in the last decade an increasing number of futures contracts have been developed that specify currencies, financial instruments or financially based indexes as the underlying commodity.

U.S. futures contracts are traded only on national futures exchanges and are standardized as to maturity date and underlying financial instrument. The principal financial futures exchanges in the United States are The Board of Trade of the City of Chicago, the Chicago Mercantile Exchange, the International Monetary Market (a division of the Chicago Mercantile Exchange), the New York Futures Exchange and the Kansas City Board of Trade. Each exchange guarantees performance under contract provisions through a clearing corporation, a nonprofit organization managed by the exchange membership, which is also responsible for handling daily accounting of deposits or withdrawals of margin. A futures commission merchant ("Broker") effects each transaction in connection with futures contracts for a commission. Futures exchanges and trading are regulated under the Commodity Exchange Act by the Commodity Futures Trading Commission ("CFTC") and National Futures Association ("NFA").

INTEREST RATE FUTURES CONTRACTS

The sale of an interest rate futures contract creates an obligation by the Fund, as seller, to deliver the type of financial instrument specified in the contract at a specified future time for a specified price. The purchase of an interest rate futures contract creates an obligation by the Fund, as purchaser, to accept delivery of the type of financial instrument specified at a specified future time for a specified price. The specific securities delivered or accepted, respectively, at settlement date, are not determined until at or near that date. The determination is in accordance with the rules of the exchange on which the futures contract sale or purchase was made.

Currently, interest rate futures contracts can be purchased or sold on 90-day U.S. Treasury bills, U.S. Treasury bonds, U.S. Treasury notes with maturities between 6 1/2 and 10 years, certificates, and 90-day Eurodollar certificates of deposit. It is expected that futures contracts trading in additional financial instruments will be authorized. The standard contract size is $100,000 for futures contracts in U.S. Treasury bonds, and U.S. Treasury notes and $1,000,000 for the other designated contracts. While U.S. Treasury bonds, U.S. Treasury bills and U.S. Treasury notes are backed by the full faith and credit of the U.S. government; the futures contracts in U.S. government securities are not obligations of the U.S. Treasury.

INDEX BASED FUTURES CONTRACTS

It is expected that bond index and other financially based index futures contracts will be developed in the future. It is anticipated that such index based futures contracts will be structured in the same way as stock index futures contracts, but will be measured by changes in interest rates, related indexes or other measures, such as the consumer price index. In the event that such futures contracts are developed, the Fund will sell interest rate index and other index based futures contracts to hedge against changes which are expected to affect the Fund's portfolio.

The purchase or sale of a futures contract differs from the purchase or sale of a security, in that no price or premium is paid or received. Instead, to initiate trading an amount of cash, cash equivalents, money market instruments, or U.S. Treasury bills equal to approximately 1 1/2% (up to 5%) of the contract amount must be deposited by the Fund with the Broker. This amount is known as initial margin. The nature of initial margin in futures transactions is different from that of margin in security transactions. Futures contract margin does not involve the borrowing of funds by the customer to finance the transactions. Rather, the initial margin is in the nature of a performance bond or good faith deposit on the contract which is returned to the Fund upon termination of the futures contract assuming all contractual obligations have been satisfied. The margin required for a particular futures contract is set by the exchange on which the contract is traded, and may be significantly modified from time to time by the exchange during the term of the contract.

Subsequent payments, called variation margin, to the Broker and from the Broker, are made on a daily basis as the value of the underlying instrument or index fluctuates making the long and short positions in the futures contract more or less valuable, a process known as mark-to-market. For example, when the Fund has purchased a futures contract and the price of the underlying financial instrument or index has risen, that position will have increased in value and the Fund will receive from the Broker a variation margin payment equal to that increase in value. Conversely, where the Fund has purchased a futures contract and the price of the underlying financial instrument or index has declined, the position would be less valuable and the Fund would be required to make a variation margin payment to the Broker. At any time prior to expiration of the futures contract, the Fund may elect to close the position. A final determination of variation margin is then made, additional cash is required to be paid to or released by the Broker, and the Fund realizes a loss or gain.

The Fund intends to enter into arrangements with its custodian and with Brokers to enable its initial margin and any variation margin to be held in a segregated account by its custodian on behalf of the Broker.

Although interest rate futures contracts by their terms call for actual delivery or acceptance of financial instruments, and index based futures contracts call for the delivery of cash equal to the difference between the closing value of the index on the expiration date of the contract and the price at which the futures contract is originally made, in most cases such futures contracts are closed out before the settlement date without the making or taking of delivery. Closing out a futures contract sale is effected by an offsetting transaction in which the Fund enters into a futures contract purchase for the same aggregate amount of the specific type of financial instrument or index and same delivery date. If the price in the sale exceeds the price in the offsetting purchase, the Fund is paid the difference and thus realizes a gain. If the offsetting purchase price exceeds the sale price, the Fund pays the difference and realizes a loss. Similarly, the closing out of a futures contract purchase is effected by an offsetting transaction in which the Fund enters into a futures contract sale. If the offsetting sale price exceeds the purchase price, the Fund realizes a gain. If the purchase price exceeds the offsetting sale price, the Fund realizes a loss. The amount of the Fund's gain or loss on any transaction is reduced or increased, respectively, by the amount of any transaction costs incurred by the Fund.

As an example of an offsetting transaction, the contractual obligations arising from the sale of one contract of September U.S. Treasury bills on an exchange may be fulfilled at any time before delivery of the contract is required (i.e., on a specified date in September, the "delivery month") by the purchase of one contract of September U.S. Treasury bills on the same exchange. In such instance, the difference between the price at which the futures contract was sold and the price paid for the offsetting purchase after allowance for transaction costs represents the profit or loss to the Fund.

There can be no assurance, however, that the Fund will be able to enter into an offsetting transaction with respect to a particular contract at a particular time. If the Fund is not able to enter into an offsetting transaction, the Fund will continue to be required to maintain the margin deposits on the contract and to complete the contract according to its terms.

OPTIONS ON CURRENCY AND OTHER FINANCIAL FUTURES

The Fund intends to purchase call and put options on currency and other financial futures contracts and sell such options to terminate an existing position. Options on currency and other financial futures contracts are similar to options on stocks except that an option on a currency or other financial futures contract gives the purchaser the right, in return for the premium paid, to assume a position in a futures contract (a long position if the option is a call and a short position if the option is a put) rather than to purchase or sell stock, currency or other financial instruments at a specified exercise price at any time during the period of the option. Upon exercise of the option, the delivery of the futures position by the writer of the option to the holder of the option will be accompanied by delivery of the accumulated balance in the writer's futures margin account. This amount represents the amount by which the market price of the futures contract at exercise exceeds, in the case of a call, or is less than, in the case of a put, the exercise price of the option on the futures contract. If an option is exercised the last trading day prior to the expiration date of the option, the settlement will be made entirely in cash equal to the difference between the exercise price of the option and value of the futures contract.

The Fund intends to use options on currency and other financial futures contracts in connection with hedging strategies. In the future the Fund may use such options for other purposes.

PURCHASE OF PUT OPTIONS ON FUTURES CONTRACTS

The purchase of protective put options on a currency or other financial futures contract is analogous to the purchase of protective puts on individual stocks, where an absolute level of protection is sought below which no additional economic loss would be incurred by the Fund. Put options may be purchased to hedge a portfolio of stocks or debt instruments or a position in the futures contract upon which the put option is based.

PURCHASE OF CALL OPTIONS ON FUTURES CONTRACTS

The purchase of a call option on a currency or other financial futures contract represents a means of obtaining temporary exposure to market appreciation at limited risk. It is analogous to the purchase of a call option on an individual stock which can be used as a substitute for a position in the stock itself. Depending on the pricing of the option compared to either the futures contract upon which it is based, or upon the price of the underlying financial instrument or index itself, the purchase of a call option may be less risky than the ownership of the interest rate or index based futures contract or the underlying securities. Call options on currency and other financial futures contracts may be purchased to hedge against an interest rate increase or a market advance when the Fund is not fully invested.

USE OF NEW INVESTMENT TECHNIQUES INVOLVING COMMODITY FUTURES CONTRACTS OR RELATED OPTIONS

The Fund may employ new investment techniques involving currency and other financial futures contracts and related options. The Fund intends to take advantage of new techniques in these areas that may be developed from time to time and that are consistent with the Fund's investment objective. The Fund believes that no additional techniques have been identified for employment by the Fund in the foreseeable future other than those described above.

LIMITATIONS ON PURCHASE AND SALE OF FUTURES CONTRACTS AND RELATED OPTIONS ON SUCH FUTURES CONTRACTS

The Fund will not enter into a futures contract if, as a result thereof, more than 5% of the Fund's total assets (taken at market value at the time of entering into the contract) would be committed to margin deposits on such futures contracts.

The Fund intends that its futures contracts and related options transactions will be entered into for traditional hedging purposes. That is, futures contracts will be sold to protect against a decline in the price of securities that the Fund owns or futures contracts will be purchased to protect the Fund against an increase in the price of securities it intends to purchase. The Fund does not intend to enter into futures contracts for speculation.

In instances involving the purchase of futures contracts by the Fund, an amount of cash and cash equivalents equal to the market value of the futures contracts will be deposited in a segregated account with the Fund's custodian and/or in a margin account with a Broker to collateralize the position and thereby insure that the use of such futures is unleveraged.

FEDERAL INCOME TAX TREATMENT

For federal income tax purposes, the Fund is required to recognize as income for each taxable year its net unrealized gains and losses on futures contracts as of the end of the year as well as those actually realized during the year. Any gain or loss recognized with respect to a futures contract is considered to be 60% long term and 40% short term, without regard to the holding period of the contract. In the case of a futures transaction classified as a "mixed straddle," the recognition of losses may be deferred to a later taxable year. The federal income tax treatment of gains or losses from transactions in options on futures is unclear.

In order for the Fund to continue to qualify for federal income tax treatment as a regulated investment company, at least 90% of its gross income for a taxable year must be derived from qualifying income. Any net gain realized from the closing out of futures contracts, for purposes of the 90% requirement, will be qualifying income. In addition, gains realized on the sale or other disposition of securities held for less than three months must be limited to less than 30% of the Fund's annual gross income. The 1986 Tax Act added a provision which effectively treats both positions in certain hedging transactions as a single transaction for the purpose of the 30% requirement. The provision provides that, in the case of any "designated hedge," increases and decreases in the value of positions of the hedge are to be netted for the purposes of the 30% requirement. However, in certain situations, in order to avoid realizing again within a three month period, the Fund may be required to defer the closing out of a contract beyond the time when it would otherwise be advantageous to do so.

RISKS OF FUTURES CONTRACTS

Currency and other financial futures contracts prices are volatile and are influenced, among other things, by changes in stock prices, market conditions, prevailing interest rates and anticipation of future stock prices, market movements or interest rate changes, all of which in turn are affected by economic conditions, such as government fiscal and monetary policies and actions, and national and international political and economic events.

At best, the correlation between changes in prices of futures contracts and of the securities being hedged can be only approximate. The degree of imperfection of correlation depends upon circumstances, such as variations in speculative market demand for futures contracts and for securities, including technical influences in futures contracts trading; and differences between the securities being hedged and the financial instruments and indexes underlying the standard futures contracts available for trading, in such respects as interest rate levels, maturities and creditworthiness of issuers, or identities of securities comprising the index and those in the Fund's portfolio. A decision of whether, when and how to hedge involves the exercise of skill and judgment, and even a well-conceived hedge may be unsuccessful to some degree because of market behavior or unexpected interest rate trends.

Because of the low margin deposits required, futures trading involves an extremely high degree of leverage. As a result, a relatively small price movement in a futures contract may result in immediate and substantial loss, as well as gain, to the investor. For example, if at the time of purchase, 10% of the value of the futures contract is deposited as margin, a 10% decrease in the value of the futures contract would result in a total loss of the margin deposit, before any deduction for the transaction costs, if the account were then closed out, and a 15% decrease would result in a loss equal to 150% of the original margin deposit. Thus, a purchase or sale of a futures contract may result in losses in excess of the amount invested in the futures contract. However, the Fund would presumably have sustained comparable losses if, instead of entering into the futures contract, it had invested in the underlying financial instrument. Furthermore, in order to be certain that the Fund has sufficient assets to satisfy its obligations under a futures contract, the Fund will establish a segregated account in connection with its futures contracts which will hold cash or cash equivalents equal in value to the current value of the underlying instruments or indices less the margins on deposit.

Most U.S. futures exchanges limit the amount of fluctuation permitted in futures contract prices during a single trading day. The daily limit establishes the maximum amount that the price of a futures contract may vary either up or down from the previous day's settlement price at the end of a trading session. Once the daily limit has been reached in a particular type of contract, no trades may be made on that day at a price beyond that limit. The daily limit governs only price movement during a particular trading day and therefore does not limit potential losses because the limit may prevent the liquidation of unfavorable positions. Futures contract prices have occasionally moved to the daily limit for several consecutive trading days with little or no trading, thereby preventing prompt liquidation of futures positions and subjecting some futures traders to substantial losses.

RISKS OF OPTIONS ON FUTURES CONTRACTS

In addition to the risks described above for currency and other financial futures contracts, there are several special risks relating to options on futures contracts. The ability to establish and close out positions on such options will be subject to the development and maintenance of a liquid secondary market. There is no assurance that a liquid secondary market will exist for any particular contract or at any particular time. The Fund will not purchase options on any futures contract unless and until it believes that the market for such options has developed sufficiently that the risks in connection with such options are not greater than the risks in connection with the futures contracts. Compared to the use of futures contracts, the purchase of options on such futures involves less potential risk to the Fund because the maximum amount at risk is the premium paid for the options (plus transaction costs). However, there may be circumstances when the use of an option on a futures contract would result in a loss to the Fund, even though the use of a futures contract would not, such as when there is no movement in the level of the futures contract.

FOREIGN CURRENCY TRANSACTIONS

The Fund may invest in securities denominated in foreign currencies, and the Fund temporarily may hold funds in foreign currencies. Thus, the Fund's share value will be affected by changes in exchange rates.

FORWARD CURRENCY CONTRACTS

As one way of managing exchange rate risk, the Fund may engage in forward currency exchange contracts (agreements to purchase or sell currencies at a specified price and date). Under the contract, the exchange rate for the transaction (the amount of currency the Fund will deliver or receive when the contract is completed) is fixed when the Fund enters into the contract. The Fund usually will enter into these contracts to stabilize the U.S. dollar value of a security it has agreed to buy or sell. The Fund also may use these contracts to hedge the U.S. dollar value of a security it already owns, particularly if the Fund expects a decrease in the value of the currency in which the foreign security is denominated. Although the Fund will attempt to benefit from using forward contracts, the success of its hedging strategy will depend on Keystone's ability to predict accurately the future exchange rates between foreign currencies and the U.S. dollar. The value of the Fund's investments denominated in foreign currencies will depend on the relative strength of those currencies and the U.S. dollar, and the Fund may be affected favorably or unfavorably by changes in the exchange rate or exchange control regulations between foreign currencies and the dollar. Changes in foreign currency exchange rates also may affect the value of dividends and interest earned, gains and losses realized on the sale of securities and net investment income and gains, if any, to be distributed to shareholders by the Fund.

CURRENCY FUTURES CONTRACTS

Currency futures contracts are bilateral agreements under which two parties agree to take or make delivery of a specified amount of a currency at a specified future time for a specified price. Trading of currency futures contracts in the United States is regulated under the Commodity Exchange Act by the CFTC and NFA. Currently the only national futures exchange on which currency futures are traded is the International Monetary Market of the Chicago Mercantile Exchange. Foreign currency futures trading is conducted in the same manner and subject to the same regulations as trading in interest rate and index based futures. The Fund intends to only engage in currency futures contracts for hedging purposes, and not for speculation. The Fund may engage in currency futures contracts for other purposes if authorized to do so by the Board. The hedging strategies that will be used by the Fund in connection with foreign currency futures contracts are similar to those described above for forward foreign currency exchange contracts.

Currently, currency futures contracts for the British Pound Sterling, Canadian Dollar, Dutch Guilder, Deutsche Mark, Japanese Yen, Mexican Peso, Swiss Franc and French Franc can be purchased or sold for U.S. dollars through the International Monetary Market. It is expected that futures contracts trading in additional currencies will be authorized. The standard contract sizes are L125,000 for the Pound, 125,000 for the Guilder, Mark and Swiss Francs, C$100,000 for the Canadian Dollar, Y12,500,000 for the Yen, and 1,000,000 for the Peso. In contrast to Forward Currency Exchange Contracts, which can be traded at any time, only four value dates per year are available, the third Wednesday of March, June, September and December.

FOREIGN CURRENCY OPTIONS TRANSACTIONS

Foreign currency options (as opposed to futures) are traded in a variety of currencies in both the United States and Europe. On the Philadelphia Stock Exchange, for example, contracts for half the size of the corresponding futures contracts on the Chicago Board Options Exchange are traded with up to nine months maturity in Marks, Sterling, Yen, Swiss Francs and Canadian Dollars. Options can be exercised at any time during the contract life and require a deposit subject to normal margin requirements. Since a futures contract must be exercised, the Fund must continually make up the margin balance. As a result, a wrong price move could result in the Fund losing more than the original investment as it cannot walk away from the futures contract as it can an option contract.

The Fund will purchase call and put options and sell such options to terminate an existing position. Options on foreign currency are similar to options on stocks except that an option on an interest rate and/or index based futures contract gives the purchaser the right, in return for the premium paid, to purchase or sell foreign currency, rather than to purchase or sell stock, at a specified exercise price at any time during the period of the option.

The Fund intends to use foreign currency option transactions in connection with hedging strategies.

PURCHASE OF PUT OPTIONS ON FOREIGN CURRENCIES

The purchase of protective put options on a foreign currency is analogous to the purchase of protective puts on individual stocks, where an absolute level of protection is sought below which no additional economic loss would be incurred by the Fund. Put options may be purchased to hedge a portfolio of foreign stocks or foreign debt instruments or a position in the foreign currency upon which the put option is based.

PURCHASE OF CALL OPTIONS ON FOREIGN CURRENCIES

The purchase of a call option on foreign currency represents a means of obtaining temporary exposure to market appreciation at limited risk. It is analogous to the purchase of a call option on an individual stock which can be used as a substitute for a position in the stock itself. Depending on the pricing of the option compared to either the foreign currency upon which it is based, or upon the price of the foreign stock or foreign debt instruments, the purchase of a call option may be less risky than the ownership of the foreign currency or the foreign securities. The Fund would purchase a call option on a foreign currency to hedge against an increase in the foreign currency or a foreign market advance when the Fund is not fully invested.

The Fund may employ new investment techniques involving forward foreign currency exchange contracts, foreign currency futures contracts and options on foreign currencies in order to take advantage of new techniques in these areas that may be developed from time to time and that are consistent with the Fund's investment objective. The Fund believes that no additional techniques have been identified for employment by the Fund in the foreseeable future other than those described above.

CURRENCY TRADING RISKS

Currency exchange trading may involve significant risks. The four major types of risk the Fund faces are exchange rate risk, interest rate risk, credit risk and country risk.

EXCHANGE RATE RISK

Exchange rate risk results from the movement up and down of foreign currency values in response to shifting market supply and demand. When the Fund buys or sells a foreign currency, an exposure called an open position is created. Until the time that position can be "covered" by selling or buying an equivalent amount of the same currency, the Fund is exposed to the risk that the exchange rate might move against it. Since exchange rate changes can readily move in one direction, a position carried overnight or over a number of days involves greater risk than one carried a few minutes or hours. Techniques such as foreign currency forward and futures contracts and options on foreign currency are intended to be used by the Fund to reduce exchange rate risk.

MATURITY GAPS AND INTEREST RATE RISK

Interest rate risk arises whenever there are mismatches or gaps in the maturity structure of the Fund's foreign exchange currency holdings, which is the total of its outstanding spot and forward or futures contracts.

Foreign currency transactions often involve borrowing short term and lending longer term to benefit from the normal tendency of interest rates to be higher for longer maturities. However in foreign exchange trading, while the maturity pattern of interest rates for one currency is important, it is the differential between interest rates for two currencies that is decisive.

CREDIT RISK

Whenever the Fund enters into a foreign exchange contract, it faces a risk, however small, that the counterparty will not perform under the contract. As a result there is a credit risk, although no extension of "credit" is intended. To limit credit risk, the Fund intends to evaluate the creditworthiness of each other party. The Fund does not intend to trade more than 5% of its net assets under foreign exchange contracts with one party.

Credit risk exists because the Fund's counterparty may be unable or unwilling to fulfill its contractual obligations as a result of bankruptcy or insolvency or when foreign exchange controls prohibit payment. In any foreign exchange transaction, each party agrees to deliver a certain amount of currency to the other on a particular date. In establishing its hedges the Fund relies on each contract being completed. If the contract is not performed, then the Fund's hedge is eliminated, and the Fund is exposed to any changes in exchange rates since the contract was originated. To put itself in the same position it would have been in had the contract been performed, the Fund must arrange a new transaction. However, the new transaction may have to be arranged at an adverse exchange rate. The trustee for a bankrupt company may elect to perform those contracts that are advantageous to the company but disclaim those contracts that are disadvantageous, resulting in losses to the Fund.

Another form of credit risk stems from the time zone differences between the U.S. and foreign nations. If the Fund sells sterling it generally must pay pounds to a counterparty earlier in the day than it will be credited with dollars in New York. In the intervening hours, the buyer can go into bankruptcy or can be declared insolvent. Thus, the dollars may never be credited to the Fund.

COUNTRY RISK

At one time or another, virtually every country has interfered with international transactions in its currency. Interference has taken the form of regulation of the local exchange market, restrictions on foreign investment by residents or limits on inflows of investment funds from abroad. Governments take such measures for example to improve control over the domestic banking system or to influence the pattern of receipts and payments between residents and foreigners. In those cases, restrictions on the exchange market or on international transactions are intended to affect the level or movement of the exchange rate. Occasionally a serious foreign exchange shortage may lead to payment interruptions or debt servicing delays, as well as interference in the exchange market. It has become increasingly difficult to distinguish foreign exchange or credit risk from country risk.

Changes in regulations or restrictions usually do have an important exchange market impact. Most disruptive are changes in rules that interfere with the normal payments mechanism. If government regulations change and a counterparty is either forbidden to perform or is required to do something extra, then the Fund might be left with an unintended open position or an unintended maturity mismatch. Dealing with such unintended long or short positions could result in unanticipated costs to the Fund.

Other changes in official regulations influence international investment transactions. If one of the factors affecting the buying or selling of a currency changes, the exchange rate is likely to respond. Changes in such controls often are unpredictable and can create a significant exchange rate response.

Many major countries have moved toward liberalization of exchange and payments restrictions in recent years or accepted the principle that restrictions should be relaxed. A few industrial countries have moved in the other direction. Important liberalizations were carried out by Switzerland, the United Kingdom and Japan. They dismantled mechanisms for restricting either foreign exchange inflows (Switzerland), outflows (Britain) or elements of both (Japan). By contrast, France and Mexico have recently tightened foreign exchange controls.

Overall, many exchange markets are still heavily restricted. Several countries limit access to the forward market to companies financing documented export or import transactions in an effort to insulate the market from purely speculative activities. Some of these countries permit local traders to enter into forward contracts with residents but prohibit certain forward transactions with nonresidents. By comparison, other countries have strict controls on exchange transactions by residents, but permit free exchange transactions between local traders and non-residents. A few countries have established tiered markets, funneling commercial transactions through one market and financial transactions through another. Outside the major industrial countries, relatively free foreign exchange markets are rare and controls on foreign currency transactions are extensive.

Another aspect of country risk has to do with the possibility that the Fund may be dealing with a foreign trader whose home country is facing a payments problem. Even though the foreign trader intends to perform on its foreign exchange contracts, the contracts are tied to other external liabilities the country has incurred. As a result performance may be delayed, and can result in unanticipated cost to the Fund. This aspect of country risk is a major element in the Fund's credit judgment as to with whom it will deal and in what amounts.

Keystone Tax Free Fund
SCHEDULE OF INVESTMENTS--December 31, 1994

	Coupon Rate	Maturity Date	Principal Amount	Market Value
MUNICIPAL BONDS (98.5%)				
ALASKA				
Alaska State Housing Finance Corp., Series 1993 A	5.400%	12/01/2023	$ 5,000,000	$ 3,914,000
North Slope Borough, Alaska, General Obligation Refunding, Series G	8.350	06/30/1998	2,000,000	2,160,340
North Slope Borough, Alaska, General Obligation, Series A (MBIA)	5.900	06/30/2003	3,000,000	2,975,250
ARIZONA				
Chandler, Arizona, Water and Sewer (FGIC)	6.750	07/01/2006	850,000	882,028
Maricopa County, Arizona, Industrial Development Authority, Hospital Facilities Revenue, Samaritan Health Services (Crossover refunded)	9.250	12/01/2015	10,715,000	11,293,074
Maricopa County, Arizona, University School District (MBIA)	8.125	01/01/2010	6,000,000	6,763,440
Phoenix, Arizona, Street and Highway User, Series 1992 A (FGIC) (effective yield 5.95%) (a)	0.000	07/01/2013	2,500,000	708,100
Pima County, Arizona, Industrial Development Authority, Health Care Corp., Carandolet St. Joseph and St. Mary Hospitals (MBIA)	8.000	07/01/2013	3,385,000	3,669,679
Pima County, Arizona, Industrial Development Authority, Irvington Project (FSA)	7.250	07/15/2010	10,000,000	10,389,400
ARKANSAS				
Arkansas State Development Finance Authority, SFMR Refunding	8.000	08/15/2011	1,820,000	1,920,209
CALIFORNIA				
California Health Facilities Financing, St. Francis Medical Center, Series A	5.500	10/01/2009	200,000	178,434
California State Public Works Board (AMBAC)	5.250	12/01/2013	1,850,000	1,541,605
California State Public Works Board, Various University California Projects, Series B	5.500	06/01/2019	350,000	281,271
California State Public Works, Board Lease Department Correctional State Prison, Series E	5.500	06/01/2015	3,700,000	3,041,548
Eden Township, California, Hospital District	7.400	11/01/2019	5,615,000	5,158,557
Fontana, California, Public Financing Authority, Tax Allocation, Series A (MBIA)	5.000	09/01/2020	295,000	226,767
Fresno, California, Health Facility, Holy Cross Health Systems (MBIA)	5.625	12/01/2015	7,000,000	5,976,320
Loma Linda, California, Refunding Loma Linda University Medical Center C (MBIA)	5.375	12/01/2022	85,000	69,022
Los Angeles County, California, Transportation Commission, Series A (MBIA)	6.250	07/01/2013	6,000,000	5,678,220
Los Angeles, California, Convention and Exhibition Center Authority Lease (MBIA)	5.125	08/15/2013	5,000,000	4,107,700
Los Angeles, California, Public Works Finance Authority, Multi Capital Facilities Project (MBIA)	5.250	12/01/2016	5,000,000	4,054,000
Moulton Niguel, California, Water District Improvement Authority (MBIA)	5.250	09/01/2013	210,000	173,867
Oakland, California, Pensions, Series A (FGIC)	7.600	08/01/2021	5,015,000	5,256,823
Oakland, California, Redevelopment Agency, Tax Allocation Central District, Series A (MBIA)	5.000	09/01/2013	2,960,000	2,392,361

See Notes to Schedule of Investments.

	Coupon Rate	Maturity Date	Principal Amount	Market Value
California (continued)				
Pittsburg, California, Redevelopment Agency, Tax Allocation Refunding, Los Medanos Project, Series A (AMBAC)	5.000%	08/01/2013	$ 4,520,000	$ 3,630,916
San Diego, California, Sewer Authority, Series A (AMBAC)	5.000	05/15/2013	975,000	784,270
San Joaquin Hills, California, Transportation Corridor Agency, Toll Road Revenue	7.000	01/01/2030	5,705,000	4,893,007
San Joaquin Hills, California, Transportation Corridor Agency, Toll Road Revenue	6.750	01/01/2032	5,000,000	4,137,300
Southern California Public Power Authority, Power Project Revenue, Series A	5.500	07/01/2012	2,300,000	1,970,916
Southern California Public Power Authority, Power Project Revenue	5.000	07/01/2015	4,600,000	3,596,878

University of California, Multiple Purpose Projects, Series C (AMBAC)	5.000	09/01/2013	1,675,000	1,341,725
University of California, Multiple Purpose Projects, Series C (AMBAC)	5.000	09/01/2014	7,525,000	5,989,373
University of California, Refunding Multiple Purpose Project, Series B (MBIA)	5.000	09/01/2016	2,000,000	1,569,680
Walnut Creek, California, John Muir Medical Center (MBIA)	5.000	02/15/2016	350,000	274,565
COLORADO				
City and County of Denver, Colorado, Airport System, Series A	8.500	11/15/2023	1,750,000	1,762,390
City and County of Denver, Colorado, Airport System, Series A	7.000	11/15/1999	2,000,000	1,969,100
City and County of Denver, Colorado, Airport System, Series A	7.500	11/15/2023	5,625,000	5,184,113
City and County of Denver, Colorado, Airport System, Series A	8.750	11/15/2023	16,380,000	16,760,671
City and County of Denver, Colorado, Airport System, Series A	8.000	11/15/2025	525,000	506,819
City and County of Denver, Colorado, Airport System, Series C	6.650	11/15/2005	5,980,000	5,393,422
City and County of Denver, Colorado, Airport System, Series C	6.000	12/01/2025	3,000,000	3,017,640
City and County of Denver, Colorado, Airport System, Series D	7.750	11/15/2021	12,250,000	11,701,812
Colorado Health Facilities Authority, Rocky Mountain Adventist Health Care	6.625	02/01/2022	3,000,000	2,537,520
Larimer County, Colorado, School District (MBIA)	7.000	12/15/2016	2,250,000	2,363,895
CONNECTICUT				
Connecticut Special Tax Obligation, Series B	6.500	10/01/2012	1,600,000	1,582,496
Connecticut State Special Tax Obligation, Series A (FGIC)	5.900	10/01/2008	6,500,000	6,185,725
Connecticut State Special Tax Obligation, Series B (FGIC)	6.000	10/01/2009	5,000,000	4,818,050
Connecticut State Special Tax Obligation, Series B (FGIC)	6.000	10/01/2010	3,980,000	3,791,627
DELAWARE				
Delaware Health Facilities Authority, Medical Center of Delaware (MBIA)	6.250	10/01/2006	6,000,000	6,096,600
DISTRICT OF COLUMBIA				
District of Columbia, General Obligation, Series E (FSA)	6.000	06/01/2011	7,000,000	6,427,050
FLORIDA				
Broward County, Florida, Resource Recovery, South Project	7.950	12/01/2008	1,920,000	2,054,630
Dade County, Florida, School District (MBIA)	5.000	08/01/2013	4,000,000	3,269,880
Dade County, Florida, Water Sewer Systems, Allegany Health Systems, St. Mary's (FGIC)	5.000	10/01/2013	11,000,000	9,160,580

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Florida (continued)

Escambia County, Florida, Pollution Control, Champion International Corp. Project	6.900%	08/01/2022	$ 1,500,000	$ 1,425,345
Florida State Board Education Capital Outlay	6.400	06/01/2019	17,000,000	16,708,450
Florida State Board Education, Capital Outlay Public Education, Series A	5.875	06/01/2012	7,465,000	6,985,971
Jacksonville, Florida, Capital Improvement Revenue Certificates, Gator Bowl Project (AMBAC)	6.000	10/01/2025	1,880,000	1,729,750
Jacksonville, Florida, Health Facility Authority, Daughters of Charity Hospital, Series A	5.000	11/15/2015	2,000,000	1,548,580
Jacksonville, Florida, Health Facility Authority, New Children's Hospital (MBIA)	7.000	06/01/2021	1,800,000	1,829,502
Jacksonville, Florida, Transportation Authority (ETM)	9.200	01/01/2015	2,000,000	2,583,300
Lee County, Florida, School Board, Certificates of Participation, Series A (FSA)	7.750	08/01/2005	3,490,000	3,836,033
Okaloosa County, Florida, Gas District, Refunding and Improvement (MBIA)	6.850	10/01/2014	1,550,000	1,589,324
Orlando-Orange County, Florida, Expressway Authority (FGIC)	8.250	07/01/2015	2,960,000	3,496,707
Palm Beach County, Florida, Criminal Justice Facilities (FGIC)	6.000	06/01/2013	1,000,000	943,410
Port St. Lucie, Florida, Utility Revenue (FGIC)	6.000	09/01/2014	5,465,000	5,180,055
St. Petersburg, Florida, Health Facilities Authority (MBIA)	7.000	12/01/2015	3,250,000	3,345,258
Tampa, Florida, Subordinate Guaranteed Entitlement, Series B (Pre-refunded)	8.500	10/01/2018	1,825,000	2,005,091
GEORGIA				
Atlanta, Georgia, General Obligation, Series A	6.000	12/01/2015	2,790,000	2,573,692
Atlanta, Georgia, General Obligation, Series A	6.000	12/01/2014	2,690,000	2,500,059
Georgia, General Obligation, Series C	5.250	04/01/2011	9,200,000	8,058,464
Metropolitan Atlanta Rapid Transit Authority, Georgia, Sales Tax (AMBAC)	6.250	07/01/2011	4,255,000	4,159,773
Monroe County, Georgia, Development Authority, Pollution Control Georgia Power Co.	10.500	09/01/2015	7,100,000	7,466,218
HAWAII				
Hawaii State Department of Budget and Finance, Special Purpose Revenue, Hawaii Electric Co. (MBIA)	7.375	12/01/2020	8,000,000	8,237,120
State of Hawaii, Airport System (MBIA)	6.450	07/01/2013	10,000,000	9,755,500
IDAHO				
Idaho Housing Finance Authority, Single Family Mortgage Bonds, Series D-1	8.000	01/01/2020	1,505,000	1,481,989
ILLINOIS				

Chicago, Illinois, Gas Supply Revenue, People's Gas Light and Coke Co., Series A	8.100	05/01/2020	6,740,000	7,201,758
Chicago, Illinois, Gas Supply Revenue, People's Gas Light and Coke Co.	7.500	03/01/2015	4,000,000	4,148,360
Chicago, Illinois, Public Building Commerce, Series A (MBIA)	5.750	12/01/2018	4,000,000	3,447,280
Cook County, Illinois, General Obligation (MBIA)	7.700	12/01/2005	5,970,000	6,663,654

See Notes to Schedule of Investments.

Illinois (continued)				
Illinois Development Finance Authority, Pollution Control Revenue, Commonwealth Edison Co.	10.625%	03/01/2015	$ 8,500,000	$ 8,733,580
	6.500	06/15/2022	9,000,000	8,686,620
Kankakee, Illinois, Sewer Revenue (FGIC)	6.875	05/01/2011	2,965,000	3,016,739
Metropolitan Pier and Exposition Authority, McCormick Place Expansion Project	7.250	06/15/2005	5,500,000	5,929,110
Robbins, Illinois, Robbins Resources Recovery, Partners A	9.250	08/15/2014	7,500,000	7,691,550
INDIANA				
Indianapolis, Indiana, Local Public Improvement Bond Bank, Series 1992D	6.750	02/01/2020	2,000,000	1,906,680
KANSAS				
Kansas City, Kansas, Utility Systems, Refunding and Improvement (FGIC)	6.250	09/01/2014	3,000,000	2,881,260
Kansas City, Kansas, Utility Systems, Refunding and Improvement (FGIC)	6.375	09/01/2023	7,150,000	6,889,955
KENTUCKY				
Carroll County, Kentucky, Kentucky Utility Company, Series A	7.450	09/15/2016	5,000,000	5,207,350
Jefferson County, Kentucky, Hospital Revenue (MBIA)	6.436	10/23/2014	6,000,000	5,859,720
Kentucky Housing Corp., Housing Revenue Bond, Series C	7.900	01/01/2021	6,295,000	6,388,859
Trimble County, Kentucky, Pollution Control, Louisville Gas and Electric Co.	7.625	11/01/2020	2,725,000	2,845,554
Trimble County, Kentucky, Pollution Control, Louisville Gas and Electric Co. Series (Pre-refunded)	7.625	11/01/2020	545,000	598,388
LOUISIANA				
Louisiana Public Facilities Authority (Crossover refunded)	8.200	12/01/2015	7,250,000	7,924,322
Louisiana State Offshore Term Authority	6.100	09/01/2002	2,500,000	2,478,450
Louisiana State Offshore Term Authority	6.250	09/01/2004	3,700,000	3,650,864
Louisiana State, Series B (MBIA)	5.625	08/01/2013	3,000,000	2,649,750
Orleans Parish, Louisiana, School Board (ETM)	9.050	02/01/2010	5,175,000	6,372,340
MAINE				
Regional Waste System, Maine	8.150	07/01/2011	2,500,000	2,705,225
MARYLAND				
Maryland State Community Development Administration, Multi-Family Housing	8.750	05/15/2012	3,345,000	3,411,432
MASSACHUSETTS				
Boston, Massachusetts, Boston City Hospital	5.750	02/15/2023	735,000	616,908
Chelsea, Massachusetts, School Project Loan Act 1948 (AMBAC)	6.000	06/15/2014	750,000	694,560
Massachusetts Bay Transportation Authority	5.400	03/01/2008	12,000,000	10,658,160
Massachusetts Bay Transportation Authority, Series A	7.000	03/01/2011	4,200,000	4,388,454
Massachusetts Bay Transportation Authority, Series A	6.250	03/01/2012	4,000,000	3,859,040
Massachusetts Bay Transportation Authority, Series B	6.200	03/01/2016	1,945,000	1,824,546
Massachusetts General Obligation, Series A	5.250	02/01/2008	8,000,000	6,855,280
Massachusetts General Obligation, Series C (FGIC) (effective yield 6.90%)(a)	0.000	12/01/2003	6,000,000	3,560,400

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Massachusetts (continued)				
Massachusetts Industrial Finance Agency, Harvard Community Health Plan, Inc.	8.125%	10/01/2017	$ 7,250,000	$ 7,575,380
Massachusetts Industrial Finance Agency, Solid Waste Disposal	9.000	08/01/2016	4,100,000	4,114,145
Massachusetts Municipal Wholesale Electric, Power Supply Systems	6.750	07/01/2008	4,000,000	4,079,680
Massachusetts State Health and Education Facilities Authority, Beth Israel Hospital (AMBAC)	5.750	07/01/2012	2,500,000	2,232,325
Massachusetts State Health and Educational Facilities (MBIA)	7.300	10/01/2018	2,000,000	2,066,560
Massachusetts State Health and Educational Facilities Authority, Cape Cod Health Systems, Series A (Connie Lee)	5.250	11/15/2021	4,000,000	3,155,320
Massachusetts State Health and Educational Facilities Authority, Children's Hospital	6.200	10/01/2016	3,890,000	3,571,409
Massachusetts State Health and Educational Facilities Authority, Lahey Clinic Medical Center, Series B	5.375	07/01/2023	1,800,000	1,453,374
Massachusetts State Health and Educational Facilities Authority, Massachusetts General Hospital, Series G (AMBAC)	5.375	07/01/2011	1,385,000	1,200,075
Massachusetts State Health and Educational Facilities Authority, Massachusetts General Hospital, Series F (AMBAC)	6.250	07/01/2012	1,000,000	958,490
Massachusetts State Health and Educational Facilities Authority, Massachusetts General Hospital, Series F (AMBAC)	6.250	07/01/2020	3,000,000	2,776,890
Massachusetts State Health and Educational Facilities Authority, New England Deaconness Hospital (AMBAC)	6.875	04/01/2022	2,980,000	2,973,116
Massachusetts State Health and Educational Facilities				

Authority, Wellesley College	5.375	07/01/2019	1,230,000	1,032,118
Massachusetts State Housing Finance Agency, Series A	6.300	10/01/2013	9,800,000	9,161,236
Massachusetts State Housing Finance Agency, Single Family Mortgage	9.500	12/01/2016	1,885,000	1,928,958
Massachusetts State Industrial Finance Agency, Pollution Control, Boston Edison Co., Series A	5.750	02/01/2014	1,000,000	831,170
Massachusetts State Special Obligation Consolidated Loan, Series B	6.000	08/01/2013	5,400,000	5,009,688
Massachusetts State Water Resources Authority, General Series A	5.900	08/01/2016	8,445,000	7,517,654
Massachusetts State, General Obligation	6.000	08/01/2014	15,000,000	13,887,750
Massachusetts State, General Obligation Consolidated Loan Series C (FGIC)	6.600	11/01/2008	8,000,000	8,170,160
Massachusetts Water Resources Authority, Series A (MBIA)	6.000	08/01/2014	1,500,000	1,365,885
Massachusetts Water Resources Authority, Series C	6.000	12/01/2011	6,480,000	6,091,459
Quincy, Massachusetts, Quincy Hospital (FSA)	5.250	01/15/2016	100,000	81,965
MICHIGAN				
Michigan State Hospital Finance Authority, Hospital Refunding (Daughters Charity Health Systems--Providence Hospital)	10.000	11/01/2015	7,960,000	8,431,550
Monroe County, Michigan, Economic Development Corp., Detroit Edison Co. (FGIC)	6.950	09/01/2022	6,000,000	6,133,560
MINNESOTA				
Dakota County, Minnesota, Housing and Redevelopment Authority, Single Family Mortgage (FGIC)	9.375	05/01/2018	35,000	35,522

See Notes to Schedule of Investments.

Minnesota (continued)				
Minnesota Housing Finance Agency, Housing Development, Residential Mortgage, Series H	6.500%	01/01/2026	$3,500,000	$3,283,385
MISSISSIPPI				
Mississippi Hospital Equipment and Facilities Authority (Connie Lee)	6.400	01/01/2007	1,000,000	993,770
MISSOURI				
Missouri Health and Educational Facilities Authority, Health Facility Refunding, Series Aa (MBIA)	6.250	06/01/2016	2,500,000	2,375,175
Missouri State Health and Educational Facilities Authority, Barnes Jewish Hospital (MBIA)	5.150	05/15/2010	5,000,000	4,330,700
Missouri State Health and Educational Facilities Authority, Barnes Jewish Hospital	5.250	05/15/2021	2,200,000	1,754,016
Phelps County, Missouri, Phelps County Regional Medical Center (Connie Lee)	6.000	05/15/2013	125,000	114,802
University of Missouri, University Improvement Systems Facilities	5.500	11/01/2023	175,000	149,074
NEBRASKA				
Nebraska Higher Education Loan Program	6.200	06/01/2013	5,800,000	5,365,522
NEVADA				
Clark County, Nevada, General Obligation, Series A (AMBAC)	7.500	06/01/2009	4,000,000	4,363,840
Clark County, Nevada, School District, Series A (MBIA)	6.750	03/01/2007	3,000,000	3,094,470
NEW JERSEY				
New Jersey Building Authority, State Building	5.000	06/15/2014	1,250,000	1,016,600
New Jersey Health Care Facilities Financing Authority, Jersey Shore Medical Center (AMBAC)	6.125	07/01/2012	1,000,000	947,910
New Jersey Health Care Facilities Financing Authority, Kimball Medical Center, Series C	8.000	07/01/2013	3,000,000	3,050,430
New Jersey Health Care Facilities Financing Authority, General Hospital Center of Passaic, Inc. (Pre-refunded)	10.375	07/01/2014	3,850,000	4,028,563
New Jersey Health Care Facilities Financing Authority, Our Lady of Lourdes Medical Center (Pre-refunded)	9.750	02/01/2015	4,350,000	4,457,749
New Jersey Health Care Facilities Financing Authority, General Hospital Center at Passaic, Inc. (Pre-refunded)	9.625	08/01/2025	7,500,000	7,855,200
New Jersey Health Care Facilities Financing Authority, General Hospital Center at Passaic, Inc. (Pre-refunded)	10.125	07/01/2002	1,800,000	1,899,684
New Jersey Health Care Facilities Financing Authority, Jersey Shore Medical Center (AMBAC)	6.250	07/01/2016	3,000,000	2,869,890
New Jersey Health Care Facilities Financing Authority, St. Elizabeth's Hospital, Series B	7.750	07/01/1998	1,450,000	1,462,180
Newark, New Jersey, Board Education (MBIA)	5.875	12/15/2015	2,500,000	2,284,225
NEW MEXICO				
City of Albuquerque, New Mexico, Hospital System, Series A (MBIA)	6.375	08/01/2007	1,500,000	1,496,115
Santa Fe, New Mexico, Series A (AMBAC)	6.300	06/01/2024	4,000,000	3,775,560

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NEW YORK				
Battery Park City Authority, New York, Refunding, Series A	5.000%	11/01/2013	$ 3,715,000	$ 2,944,695
Battery Park City Authority, New York, Refunding Bonds	5.250	11/01/2017	1,000,000	797,500
Metropolitan Transportation Authority, New York, Commuter Facilities, Series A (MBIA)	6.125	07/01/2014	2,990,000	2,809,942
Metropolitan Transportation Authority, New York, Commuter Facilities, Series O (MBIA)	6.250	07/01/2014	4,000,000	3,813,200
Nassau County, New York, Refunding Combined Sewer Districts, Series G (MBIA)	5.400	01/15/2012	2,000,000	1,726,040

New York City, New York, General Obligation, Series A	7.750	08/15/2014	5,460,000	5,681,676
New York City, New York, General Obligation, Fiscal 1992, Series A	7.750	08/15/2008	6,000,000	6,316,140
New York City, New York, General Obligation, Fiscal 1992, Series A	7.750	08/15/2015	3,250,000	3,365,017
New York City, New York, General Obligation, Series A (FGIC)	5.750	08/01/2010	390,000	351,094
New York City, New York, General Obligation, Series D	7.700	02/01/2009	3,000,000	3,114,810
New York City, New York, General Obligation, Series D (MBIA)	6.000	08/01/2006	285,000	276,869
New York City, New York, General Obligation, Series H	7.000	02/01/2008	2,150,000	2,147,162
New York City, New York, General Obligation, Series S	7.500	02/01/2007	1,800,000	1,879,344
New York City, New York, Industrial Special Facility Terminal One Group Association Project	6.000	01/01/2015	2,500,000	2,212,875
New York City, New York, Municipal Water Finance Authority	5.625	06/15/2011	5,800,000	5,134,682
New York City, New York, Municipal Water Finance Authority, Water and Sewer System (FGIC)	7.000	06/15/2015	6,000,000	6,127,800
New York Energy Research and Development Authority Consolidated Edison Project	7.750	01/01/2024	2,900,000	2,954,752
New York State Care Facilities, New York Hospital, Series A	6.800	08/15/2024	2,000,000	2,007,140
New York State Dormitory Authority, City University Educational Facilities (FGIC)	7.000	07/01/2009	4,980,000	5,248,123
New York State Dormitory Authority, University of Rochester Strong Memorial (MBIA)	5.500	07/01/2021	400,000	335,612
New York State Dormitory Authority, City University (AMBAC)	6.250	07/01/2016	5,000,000	4,799,750
New York State Dormitory Authority, State University Educational Facilities	5.875	05/15/2011	13,100,000	11,749,914
New York State Dormitory Authority, State University Educational Facilities	6.375	05/15/2014	2,760,000	2,560,397
New York State Energy Research and Development Authority	7.150	02/01/2022	7,250,000	6,538,485
New York State Environmental Facilities Corp., State Water Pollution Control (New York City Water Finance Authority)	6.875	06/15/2014	16,400,000	14,707,192
New York State Environmental Facilities Corp., State Water Pollution Control (New York City Water Finance Authority)	6.875	06/15/2010	5,000,000	5,045,900
New York State Housing Finance Agency, Multi-family Mortgage, Series B (AMBAC)	6.250	08/15/2014	4,440,000	4,148,026
New York State Local Government Assistance Corp. (Pre-refunded)	6.750	04/01/2021	900,000	961,695
New York State Medical Care Facilities Finance (FGIC)	6.375	08/15/2014	3,550,000	3,416,626

See Notes to Schedule of Investments.

New York (continued)				
New York State Medical Care Facilities, Mental Health (FGIC)	5.500%	08/15/2021	$ 165,000	$ 139,273
New York State Medical Care Facilities, Mental Health Facility, Series F (FSA)	5.375	02/15/2014	1,000,000	846,600
New York State Mortgage Agency	6.900	04/01/2015	4,500,000	4,506,345
New York State Urban Development Corp., Refunding Correctional Facilities, Series A	6.500	01/01/2010	10,000,000	9,622,900
New York Urban Development Corp., Correctional Facilities, Series A	7.500	04/01/2011	8,000,000	8,286,400
Onondaga County, New York, Resource Recovery Agency	6.875	05/01/2006	9,600,000	9,031,776
Port Authority of New York and New Jersey	6.000	12/01/2015	2,060,000	1,883,376
Triborough Bridge and Tunnel Authority, New York, Special Obligation	6.625	01/01/2012	8,500,000	8,579,985
NORTH CAROLINA				
North Carolina Eastern Municipal Power Agency, Power Systems	7.250	01/01/2007	1,000,000	1,028,150
North Carolina Eastern Municipal Power Agency, Power Systems	6.250	01/01/2012	5,100,000	4,609,176
North Carolina Eastern Municipal Power Agency, Power Systems	7.000	01/01/2013	6,000,000	5,902,020
North Carolina Eastern Municipal Power Agency, Power Systems	6.500	01/01/2017	4,050,000	3,713,445
North Carolina Eastern Municipal Power Agency, Power Systems	6.500	01/01/2018	1,210,000	1,117,786
North Carolina Eastern Municipal Power Agency, Power Systems, Series B	7.000	01/01/2008	5,000,000	4,978,900
North Carolina Eastern Municipal Power Agency, Power Systems, Series C	7.000	01/01/2007	1,750,000	1,735,790
North Carolina Eastern Municipal Power Agency, Power Systems	7.250	01/01/2007	18,000,000	18,989,280
Raleigh-Durham, North Carolina, Airport Authority, Special Facility, American Airlines, Inc. Project	9.625	11/01/2015	13,500,000	14,083,065
NORTH DAKOTA				
North Dakota State Housing Finance Agency, Single Family Mortgage	8.375	07/01/2021	710,000	728,985
OHIO				
Cleveland, Ohio, Public Power Systems, First Mortgage, Series A (MBIA)	7.000	11/15/2016	4,000,000	4,114,680
Cleveland, Ohio, Public Power Systems, First Mortgage, Series A (MBIA)	7.000	11/15/2024	1,000,000	1,024,540
Columbus, Ohio, General Obligation	12.375	02/15/2006	1,285,000	1,890,338
Ohio Housing Finance Agency, Single Family Mortgage (FGIC)	9.000	01/15/2009	45,000	44,819
Ohio State Higher Educational Facility Commission (MBIA)	6.125	11/15/2017	1,000,000	934,070
Ohio State Water Development Authority (Pre-refunded)	9.250	12/01/2012	505,000	528,578
Ohio State Water Development Authority (AMBAC)	9.250	12/01/2012	215,000	224,836
Ohio State Water Development Authority (AMBAC)	9.375	12/01/2018	725,000	755,450
OREGON				
Portland, Oregon, Sewer Systems, Series A (FSA)	6.250	06/01/2015	1,000,000	964,070
PENNSYLVANIA				
Allegheny County, Pennsylvania, Industrial Development Authority, Nursing Home	5.700	09/01/2030	2,000,000	1,613,740

Beaver County, Pennsylvania, Ohio Edison (FGIC)	7.000	06/01/2021	4,390,000	4,508,003
Chester County, Pennsylvania, Health and Education Facilities Authority, Mainline Health System	5.500	05/15/2015	6,240,000	5,116,925
Delaware County, Pennsylvania, Authority Health Care, Mercy Health Company of Southeastern, PA (Connie Lee)	5.375	11/15/2023	5,000,000	4,028,500

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Pennsylvania (continued)

Delaware County, Pennsylvania, Hospital Revenue, Crozier Chester Medical Center (Pre-refunded)	7.500%	12/15/2020	$2,545,000	$2,822,787
Delaware County, Pennsylvania, Industrial Development Authority, Resource Recovery Project (LOC Security Pacific)	8.100	12/01/2013	4,000,000	4,223,080
Guthrie Health Systems, Care Facility of Sayre, Pennsylvania (AMBAC)	7.100	03/01/2017	1,250,000	1,281,637
Hampden Township, Pennsylvania, Sewer Authority (FGIC) (effective yield 6.95%) (a)	0.000	04/01/2005	1,410,000	748,104
Lehigh County, Pennsylvania, Pennsylvania Power & Light Co. Project, Series A (MBIA)	6.400	11/01/2021	1,500,000	1,442,250
North Penn, Pennsylvania, Water Authority (FGIC)	6.875	11/01/2019	2,500,000	2,515,625
Northumberland County, Pennsylvania, Authority Prisons Lease (Pre-refunded)	7.750	10/15/2004	2,110,000	2,349,759
Pennsylvania Economic Development Financing Authority, Resources Recovery, Northampton Project	6.400	01/01/2009	4,000,000	3,473,360
Pennsylvania Economic Development Financing Authority, Resources Recovery, Colver Project, Series D	7.050	12/01/2010	3,000,000	2,832,360
Pennsylvania Economic Development Financing Authority, Resources Recovery, Northampton Project	6.600	01/01/2019	9,000,000	7,647,930
Pennsylvania Economic Development Financing Authority, Resources Recovery, Colver Project, Series D	7.125	12/01/2015	1,000,000	934,890
Pennsylvania Economic Development Financing Authority, Resources Recovery, Northampton Project	6.500	01/01/2013	5,500,000	4,732,420
Pennsylvania Housing Finance Agency, Single Family Mortgage, Series T	7.750	10/01/2009	4,000,000	4,077,280
Pennsylvania Housing Finance Agency, Single Family Mortgage, Section 8	8.200	07/01/2024	6,000,000	6,370,680
Pennsylvania Housing Finance Agency, Single Family Mortgage, Series 34 A	6.850	04/01/2016	500,000	499,350
Pennsylvania Intergovernmental Cooperative Authority, Philadelphia Funding (FGIC)	6.750	06/15/2021	2,410,000	2,403,879
Pennsylvania State Higher Educational Facilities Authority, Thomas Jefferson University	5.300	11/01/2015	1,000,000	816,310
Pennsylvania State Industrial Development Authority, Series 1994 (AMBAC)	6.000	01/01/2012	1,000,000	926,460
Pennsylvania State, General Obligation	5.375	05/01/2011	4,000,000	3,497,320
Pennsylvania State, General Obligation	5.375	04/15/2012	3,500,000	3,030,195
Philadelphia, Pennsylvania, Hospital and Higher Education Facilities, Graduate Health System Education Facilities Authority, Series A	7.250	07/01/2018	2,500,000	2,306,350
Philadelphia, Pennsylvania, Hospital and Higher Education Facilities, Albert Einstein Medical Center	7.000	10/01/2021	3,055,000	2,960,753
Philadelphia, Pennsylvania, Hospital and Higher Education Facilities, Community College, Series B (MBIA)	6.500	05/01/2007	280,000	282,212
Philadelphia, Pennsylvania, Hospital and Higher Education Facilities, Graduate Health System Education Facilities Authority, Series A	6.250	07/01/2018	2,000,000	1,634,040

See Notes to Schedule of Investments.

Pennsylvania (continued)

Philadelphia, Pennsylvania, Hospital and Higher Education Facilities, Temple University Authority	6.625%	11/15/2023	$ 1,725,000	$ 1,468,389
Philadelphia, Pennsylvania, Hospital and Higher Education, Chestnut Hill Hospital	6.500	11/15/2022	5,000,000	4,568,550
Philadelphia, Pennsylvania, Municipal Authority (Pre-refunded)	7.800	04/01/2018	285,000	310,220
Philadelphia, Pennsylvania, Municipal Authority (Pre-refunded)	7.800	04/01/2018	2,760,000	3,031,529
Philadelphia, Pennsylvania, Municipal Development Authority, Criminal Justice Center, Series A (MBIA)	7.100	11/15/2006	4,095,000	4,343,280
Philadelphia, Pennsylvania, Water and Wastewater	5.750	06/15/2013	2,700,000	2,297,889
Philadelphia, Pennsylvania, Water and Wastewater (FGIC)	10.000	06/15/2005	7,000,000	8,946,280
Pittsburgh, Pennsylvania, Urban Redevelopment Authority, Multi-Family Housing Mortgage, 1985 Series A	9.250	12/01/2027	3,190,000	3,269,527
Pottsville, Pennsylvania, Hospital Authority, Daughters of Charity Health Systems, Inc., Good Samaritan Hospital (Pre-refunded)	8.250	08/01/2012	2,670,000	2,907,576
Solanco, Pennsylvania, School District (FGIC)	6.300	02/15/2014	1,250,000	1,185,600
PUERTO RICO				
Puerto Rico Commonwealth, Refunding (Capital Guaranty)	6.450	07/01/2017	2,000,000	1,932,780
Puerto Rico Commonwealth, General Obligation	7.000	07/01/2010	12,000,000	12,123,720
Puerto Rico Electric Power Authority	6.000	07/01/2016	2,000,000	1,815,620
Puerto Rico Electric Power Authority, Power Revenue, Series U	6.000	07/01/2014	1,365,000	1,248,743

Puerto Rico Public Buildings Authority, Guaranteed Public Education and Health Facilities, Series M Health Facilities	5.700	07/01/2009	6,450,000	5,942,965
Puerto Rico Telephone Authority (MBIA)	5.250	01/01/2005	16,900,000	15,720,887
RHODE ISLAND				
Rhode Island State Health and Educational Building Corp., Hospital Financing Revenue, Roger Williams General Hospital	9.500	07/01/2016	4,210,000	4,345,057
Rhode Island State Industrial Facilities Corp., Marine Terminal	6.000	11/01/2014	5,000,000	4,514,800
SOUTH CAROLINA				
South Carolina State Public Service Authority, Santee Cooper, Series C (AMBAC)	5.000	01/01/2014	2,200,000	1,772,540
Sumter County, South Carolina, Hospital Facilities, The Tuomey Hospital (Pre-refunded)	10.000	10/01/2004	250,000	259,610
TENNESSEE				
Bristol, Tennessee, Health and Education Authority, Bristol Memorial Hospital (FGIC)	6.750	09/01/2010	4,200,000	4,263,378
Knox County, Tennessee, Health and Educational Facilities, Fort Sanders Hospital Alliance, Series C (MBIA)	7.250	01/01/2010	3,000,000	3,197,640
Knox County, Tennessee, Health and Educational Facilities, Fort Sanders Hospital Alliance (MBIA)	5.250	01/01/2015	3,500,000	2,930,970
Tennessee Housing Development Authority, Home Ownership Program, Issue H	7.825	07/01/2015	5,620,000	5,747,181

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TEXAS				
Austin, Texas, Utility Systems (MBIA)	5.250%	05/15/2018	$ 7,000,000	$ 5,680,850
Bear County, Texas, Health Facilities Development Corp., Revenue Refunding, Incarnate Word Health Services (Crossover refunded)	9.500	11/01/2015	8,640,000	9,132,998
Bear, Texas, Metropolitan Water District Waterworks Systems (AMBAC)	6.625	05/01/2014	1,850,000	1,828,577
Fort Bend County, Texas, Levee Improvement (MBIA)	6.900	09/01/2020	1,165,000	1,170,907
Harris County, Texas, Senior Lien Toll Road Series A (MBIA)	6.375	08/15/2024	4,000,000	3,779,040
Harris County, Texas, Flood Control District, Series B (effective yield 7.20%) (a)	0.000	10/01/2006	4,500,000	2,014,380
Harris County, Texas, Health Facilities Development Corp.	6.600	06/01/2014	5,000,000	4,626,900
Harris County, Texas, Health Facilities Development Corp., Hermann Hospital Project (MBIA)	6.375	10/01/2024	3,300,000	3,113,418
Harris County, Texas, Health Facilities Development Corp., Hermann Hospital Project (MBIA)	6.375	10/01/2017	2,480,000	2,366,490
Houston, Texas, Airport	8.200	07/01/2017	1,840,000	2,000,356
Houston, Texas, General Obligation	7.000	03/01/2008	3,000,000	3,139,620
Midland County, Texas, Hospital District, Midland Memorial Hospital	7.500	06/01/2016	600,000	568,938
Port of Corpus Christi, Texas, Industrial Development Corp., Valero Refining and Marketing Co. Project, Series A	10.250	06/01/2017	11,050,000	12,121,629
Rio Grande Valley, Texas, Health Facilities Corp., Hospital Revenue, Baptist Medical Center Project (MBIA)	8.000	08/01/2017	1,085,000	1,172,983
Rio Grande Valley, Texas, Health Facilities Corp., Hospital Revenue, Baptist Medical Center Project (Pre-refunded)	8.000	08/01/2017	5,915,000	6,498,633
San Antonio, Texas, Electric and Gas	6.000	02/01/2014	2,500,000	2,292,300
San Antonio, Texas, Electric and Gas, Series A	5.000	02/01/2014	250,000	202,685
State of Texas, General Obligation, Series B	5.700	12/01/2014	250,000	215,458
State of Texas, Veterans Housing Assistance, Series 1992, General Obligation	6.050	12/01/2012	2,695,000	2,634,362
Tarrant County, Texas, Health Facilities Development Corp., Health Systems (FGIC)	6.000	09/01/2024	1,500,000	1,349,310
Tarrant County, Texas, Housing Finance Corp., Series A (MBIA) (effective yield 7.40%) (a)	0.000	09/15/2016	6,415,000	1,383,844
Texas Housing Agency, Residential Development	8.400	01/01/2021	2,950,000	3,069,504
Texas Municipal Power Agency, Refunding Bonds (MBIA)	5.250	09/01/2012	175,000	151,337
Texas National Research Laboratory Commission Financing Corp. Lease	7.100	12/01/2021	2,390,000	2,383,929
Titus County, Texas, Water District #1, Southwest Electric Power	8.200	08/01/2011	5,500,000	6,057,370
Tomball, Texas, Hospital Authority, Tomball Regional Hospital	6.100	07/01/2008	1,860,000	1,600,474
Tomball, Texas, Hospital Authority, Tomball Regional Hospital	6.125	07/01/2023	8,000,000	6,229,680
Travis County, Texas Health Facilities, Daughters Of Charity	6.000	11/15/2022	2,000,000	1,727,140
University of Texas, University Revenue, Series B	6.750	08/15/2013	2,000,000	2,006,460
UTAH				
Intermountain Power Agency, Utah, Power Supply	7.750	07/01/2020	24,000,000	25,273,440

See Notes to Schedule of Investments.

Utah (continued)				
Intermountain Power Agency, Utah, Power Supply (Pre-refunded) (effective yield 6.25%) (a)	0.000%	07/01/2012	$20,350,000	$ 17,211,013
Intermountain Power Agency, Utah, Power Supply (ETM) (effective yield 6.80%) (a)	0.000	07/01/2020	3,000,000	396,150
Intermountain Power Agency, Utah, Power Supply, Series A				

(effective yield 7.09%) (a)	0.000	07/01/2004	8,000,000	4,438,000
Intermountain Power Agency, Utah, Special Obligation	7.875	07/01/2014	4,210,000	4,377,684
Utah State Housing Finance Agency, Single Family Mortgage	10.750	07/01/2008	70,000	71,181
Utah State Housing Finance Agency, Single Family Mortgage	7.950	07/01/2010	565,000	594,075
VIRGINIA				
Augusta County, Virginia, Industrial Development Authority, Augusta Hospital Corp. (AMBAC)	5.500	09/01/2015	2,000,000	1,715,040
Fairfax County, Virginia, Water Authority	5.000	04/01/2016	4,000,000	3,230,200
Pittsylvania County, Virginia, Industrial Development, Series A	7.500	01/01/2014	1,000,000	956,270
Virginia Housing Development Authority, Residential Mortgage, Series B (effective yield 9.97%) (a)	0.000	09/01/2014	590,000	78,287
WASHINGTON				
Washington State Health Care Facilities Authority, Multi-Care Medical Center of Tacoma (FGIC)	7.875	08/15/2011	1,300,000	1,402,271
WISCONSIN				
Wisconsin Health and Education Facilities Authority, Bellin Memorial Hospital, Inc. (Pre-refunded)	7.625	04/01/2019	5,000,000	5,464,900
Wisconsin Housing and Economic Development Authority, Home Ownership	8.000	03/01/2021	2,160,000	2,205,662
WYOMING				
Wyoming Community Development Authority, Single Family Mortgage, Series B	8.125	06/01/2021	1,765,000	1,814,049
TOTAL MUNICIPAL BONDS (Cost--$1,205,643,008)				1,179,980,518
TEMPORARY TAX-EXEMPT INVESTMENTS (0.2%)				
Dade County, Florida, Water and Sewer Systems (FGIC) (b)	4.950	10/05/2022	375,000	375,000
Sayre County, Pennsylvania, Health Care Facilities Authority, Variable Rate Demand Hospital Revenue Bonds (VHA of Pennsylvania Inc. Capital Asset Financing Program) Series 1985B (AMBAC) (b)	5.250	12/01/2020	1,125,000	1,125,000
Texas State Department Housing and Community Affairs, Multi-Family Revenue (b)	5.400	02/01/2023	465,000	465,000
TOTAL TEMPORARY TAX-EXEMPT INVESTMENTS (Cost--$1,965,000)				1,965,000
TOTAL INVESTMENTS (Cost--$1,207,608,008) (c)				1,181,945,518
OTHER ASSETS AND LIABILITIES--NET (1.3%)				15,781,378
NET ASSETS (100.0%)				$1,197,726,896

</TABLE>

(continued on next page)

Notes to Schedule of Investments:
(a) Effective yield (calculated at the date of purchase) is the annual yield at which the bond accretes until its maturity date.
(b) Variable or floating rate instruments with periodic demand features. The Fund is entitled to full payment of principal and accrued interest upon surrendering the security to the issuing agent according to the terms of the demand features.
(c) The cost of investments for federal income tax purpose amounted to $1,207,894,783. Gross unrealized appreciation and depreciation of investments, based on identified tax cost, at December 31, 1994, are as follows:

Gross unrealized appreciation	$ 20,359,452
Gross unrealized depreciation	(46,308,717)
Net unrealized depreciation	$(25,949,265)

Legend of Portfolio Abbreviations:
AMBAC--AMBAC Indemnity Corp.
ETM--Escrow to Maturity
FGIC--Federal Guaranty Insurance Co.
LOC--Line of Credit
MBIA--Municipal Bond Investors Assurance Corp.
See Notes to Schedule of Investments.

Keystone Tax Free Fund
FINANCIAL HIGHLIGHTS
(For a share outstanding throughout the year)

	Year Ended December 31, 1994	1993	1992	1991
Net asset value: Beginning of year	$ 8.12	$ 8.04	$ 8.07	$ 7.90
Income from investment operations:				
Investment income--net	0.37	0.39	0.46	0.46
Net gains (losses) on investments	(0.96)	0.48	0.12	0.36

Net commissions paid on fund share sales(b)	-0-	-0-	-0-	-0-
Total from investment operations	(0.59)	0.87	0.58	0.82
Less distributions from(a):				
Investment income--net	(0.37)	(0.39)	(0.46)	(0.46)
In excess of investment income--net	(0.06)	(0.06)	(0.04)	(0.07)
Realized capital gains--net	-0-	(0.33)	(0.11)	(0.12)
In excess of realized capital gains--net	-0-	(0.01)	-0-	-0-
Total distributions	(0.43)	(0.79)	(0.61)	(0.65)
Net asset value: End of year	$ 7.10	$ 8.12	$ 8.04	$ 8.07
Total return(c)	(7.34%)	11.15%	7.55%	10.80%
Ratios/ supplemental data				
Ratios to average net assets:				
Operating and management expenses	1.55%	1.66%	1.38%	1.75%
Investment income--net	4.92%	4.72%	5.71%	5.78%
Portfolio turnover rate	84%	76%	78%	77%
Net assets, end of year (thousands)	$1,197,727	$1,548,503	$1,453,199	$1,146,185

<TABLE>
<CAPTION>

	Year Ended December 31,					
	1990(d)	1989	1988	1987	1986	1985
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Net asset value: Beginning of year	$ 8.06	$ 8.18	$ 8.09	$ 8.85	$ 8.31	$ 7.57
Income from investment operations:						
Investment income--net	0.52	0.57	0.55	0.56	0.68	0.70
Net gains (losses) on investments	(0.01)	0.15	0.30	(0.58)	0.88	0.81
Net commissions paid on fund share sales(b)	-0-	-0-	-0-	-0-	(0.08)	(0.07)
Total from investment operations	0.51	0.72	0.85	(0.02)	1.48	1.44
Less distributions from(a):						
Investment income--net	(0.52)	(0.60)	(0.63)	(0.64)	(0.68)	(0.70)

In excess of investment income--net	(0.03)	-0-	-0-	-0-	-0-	-0-
Realized capital gains--net	(0.12)	(0.24)	(0.13)	(0.10)	(0.26)	-0-
In excess of realized capital gains--net	-0-	-0-	-0-	-0-	-0-	-0-
Total distributions	(0.67)	(0.84)	(0.76)	(0.74)	(0.94)	(0.70)
Net asset value: End of year	$ 7.90	$ 8.06	$ 8.18	$ 8.09	$ 8.85	$ 8.31
Total return(c)	6.66%	9.11%	10.89%	(0.14)%	18.26%	19.96%
Ratios/ supplemental data						
Ratios to average net assets:						
Operating and management expenses	1.18%	1.23%	1.79%	1.70%	0.83%	0.92%
Investment income--net	6.54%	6.94%	6.74%	6.80%	7.79%	8.65%
Portfolio turnover rate	64%	69%	61%	43%	44%	55%
Net assets, end of year (thousands)	$1,060,826	$901,912	$903,132	$894,768	$1,025,084	$863,720

</TABLE>

(a) Effective January 1, 1993 the Fund adopted Statement of Position 93-2: "Determination, Disclosure, and Financial Statement Presentation of Income Capital Gain and Return of Capital Distributions by Investment Companies." As a result, distribution amounts exceeding book basis investment income--net (or tax basis net income on a temporary basis) are presented as "Distributions in excess of investment income--net." Similarly, capital gain distributions in excess of book basis capital gains (or tax basis capital gains on a temporary basis) are presented as "Distributions in excess of realized capital gains." For the fiscal years ended December 31, 1992, 1991, and 1990, distributions in excess of book basis net income were presented as "distribution from paid-in capital".
(b) Prior to June 30, 1987, net commissions paid on new sales of shares under the Fund's Rule 12b-1 Distribution Plan had been treated for both financial statement and tax purposes as capital charges. On June 11, 1987, the Securities and Exchange Commission adopted a rule which required for financial statements for the periods ended on or after June 30, 1987, that net commissions paid under Rule 12b-1 be treated as operating expenses rather than capital charges. Accordingly, beginning with the year ended December 31, 1987, the Fund's financial statements reflect 12b-1 Distribution Plan expenses (i.e., shareholder servicing fees plus commissions paid net of deferred sales charges received by the Fund) as a component of net investment income.
(c) Excluding contingent deferred sales charges.
(d) Calculation based on average shares outstanding.

See Notes to Financial Statements.

Keystone Tax Free Fund
STATEMENT OF ASSETS AND LIABILITIES
December 31, 1994

Assets:	
Investments at market value (identified cost--$1,207,608,008) (Note 1)	$1,181,945,518
Cash	217,202
Receivable for:	
Investments sold	1,617,183
Fund shares sold	283,803
Interest	24,738,850
Other assets	100,602
Total assets	1,208,903,158
Liabilities (Notes 2, 4, and 5):	
Payable for:	

Income distribution	6,314,436
Investments purchased	1,997,688
Fund shares redeemed	2,777,855
Payable to Investment Adviser	58,863
Accrued reimbursable expenses	2,325
Other accrued expenses	25,095
Total liabilities	11,176,262
Net assets	$1,197,726,896
Net assets represented by:	
Paid-in capital	$1,264,955,468
Accumulated distributions in excess of investment income--net (Note 1)	(3,916,731)
Accumulated realized gains (losses) on investment transactions--net	(37,649,351)
Net unrealized appreciation (depreciation) on investments	(25,662,490)
Total net assets applicable to outstanding shares of beneficial interest ($7.10 a share on 168,806,043 shares outstanding) (Note 2)	$1,197,726,896

STATEMENT OF OPERATIONS
Year Ended December 31, 1994

Investment income (Note 1):		
Interest		$ 88,670,484
Expenses (Notes 2 and 4):		
Investment management fee and administrative services	$ 7,970,545	
Accounting services	23,917	
Trustees' fees and expenses	56,308	
Distribution Plan expenses	13,226,327	
Total expenses		21,277,097
Investment income--net (Note 1)		67,393,387
Realized and unrealized gain (loss) on investments and closed futures contracts--net (Notes 1 and 3):		
Realized gain (loss) on:		
Investments	(39,550,582)	
Closed futures contracts	1,701,424	
Realized loss on investments and closed futures contracts--net		(37,849,158)
Net unrealized appreciation (depreciation) on investments:		
Beginning of year	114,076,321	
End of year	(25,662,490)	
Change in unrealized appreciation or depreciation on investments--net		(139,738,811)
Net loss on investments		(177,587,969)
Net decrease in net assets resulting from operations		($110,194,582)

See Notes to Financial Statements.

Keystone Tax Free Fund
STATEMENTS OF CHANGES IN NET ASSETS

	Year Ended December 31, 1994	1993
Operations:		
Investment income--net (Note 1)	$ 67,393,387	$ 71,989,777
Realized gain (loss) on investments and closed futures contracts--net (Notes 1 and 3)	(37,849,158)	61,450,085
Change in unrealized appreciation or depreciation on investments--net	(139,738,811)	27,381,004
Net increase (decrease) in net assets resulting from operations	(110,194,582)	160,820,866
Distributions to shareholders from (Notes 1 and 5):		
Investment income--net	(68,740,949)	(71,989,777)
In excess of investment income--net	(10,297,613)	(11,148,339)
Realized capital gains from investment transactions--net	-0-	(61,329,277)
In excess of realized capital gains from investment transactions--net	-0-	(1,324,888)
Total distributions to shareholders	(79,038,562)	(145,792,281)
Capital share transactions (Note 2):		
Proceeds from shares sold	126,813,101	169,165,502
Payments for shares redeemed	(326,066,785)	(172,689,849)
Net asset value of shares issued in		

reinvestment of distributions from:		
Investment income--net and in excess of investment income--net	37,710,385	43,019,252
Realized gain from investment transactions--net	-0-	40,780,868
Net increase (decrease) in net assets resulting from capital share transactions	(161,543,299)	80,275,773
Total increase (decrease) in net assets	(350,776,443)	95,304,358
Net assets:		
Beginning of year	1,548,503,339	1,453,198,981
End of year [including undistributed investment income--net (accumulated distributions in excess of investment income--net) as follows: December 31, 1994--($3,916,731) December 31, 1993--$1,347,562]	$1,197,726,896	$1,548,503,339

See Notes to Financial Statements.

Keystone Tax Free Fund
NOTES TO FINANCIAL STATEMENTS
1. Significant Accounting Policies

Keystone Tax Free Fund (the "Fund") is a Massachusetts business trust for which Keystone Management, Inc. ("KMI") is the Investment Manager and Keystone Custodian Funds, Inc. ("Keystone") is the Investment Adviser. The Fund is registered under the Investment Company Act of 1940 as a diversified open-end investment company.

Keystone is a wholly-owned subsidiary of Keystone Group, Inc. ("KGI"), a Delaware corporation. KGI is privately owned by an investor group consisting of members of current and former management of Keystone. Keystone Investor Resource Center, Inc. ("KIRC"), a wholly-owned subsidiary of Keystone, is the Fund's transfer agent.

The following is a summary of significant accounting policies consistently followed by the Fund in the preparation of its financial statements. The policies are in conformity with generally accepted accounting principles.

A. Tax-exempt bonds are stated on the basis of valuations provided by a pricing service, approved by the Board of Trustees, that uses information with respect to transactions in bonds, quotations from bond dealers, market transactions in comparable securities and various relationships between securities in determining value. Non- tax-exempt securities for which market quotations are readily available are valued at the price quoted which, in the opinion of the Board of Trustees or their representative, most nearly represents their market value.

Short-term investments which are purchased with maturities of sixty days or less are valued at amortized cost (original purchase cost as adjusted for amortization of premium or accretion of discount) which when combined with accrued interest approximates market. Short- term investments maturing in more than sixty days for which market quotations are readily available are valued at current market value. Short-term investments maturing in more than sixty days when purchased which are held on the sixtieth day prior to maturity are valued at amortized cost (market value on the sixtieth day adjusted for amortization of premium or accretion of discount) which when combined with accrued interest approximates market. All other securities and other assets are valued at fair value as determined in good faith using methods prescribed by the Board of Trustees.

B. A futures contract is an agreement between two parties to buy and sell a specific amount of a commodity, security, financial instrument, or, in the case of a stock index, cash at a set price on a future date. Upon entering into a futures contract, the Fund is required to deposit with a broker an amount ("initial margin") equal to a certain percentage of the purchase price indicated in the futures contract. Subsequent payments ("variation margin") are made or received by the Fund each day, as the value of the underlying instrument or index fluctuates, and are recorded for book purposes as unrealized gains or losses by the Fund. For federal tax purposes, any futures contracts which remain open at fiscal year-end are marked-to-market and the resultant net gain or loss is included in federal taxable income. In addition to market risk the Fund is subject to the credit risk that the other party will not complete the obligations of the contract.

C. Securities transactions are accounted for on the trade date. Realized gains and losses are recorded on the identified cost basis. Interest income is recorded on the accrual basis. All premiums and original issue discounts are amortized/accreted for both financial reporting and federal income tax purposes.

D. The Fund has qualified, and intends to qualify in the future, as a regulated investment company under the Internal Revenue Code of 1986, as amended ("Internal Revenue Code"). Thus, the Fund expects to

be relieved of any federal income tax liability by distributing all of its tax basis income and net capital gains, if any, to its shareholders. The Fund intends to avoid excise tax liability by making the required distributions under the Internal Revenue Code.

E. When the Fund enters into a repurchase agreement (a purchase of securities whereby the seller agrees to repurchase the securities at a mutually agreed upon date and price) the repurchase price of the securities will generally equal the amount paid by the Fund plus a negotiated interest amount. The seller under the repurchase agreement will be required to provide securities ("collateral") to the Fund whose value will be maintained at an amount not less than the repurchase price, and which generally will be maintained at 101% of the repurchase price. The Fund monitors the value of collateral on a daily basis, and if the value of collateral falls below required levels, the Fund intends to seek additional collateral from the seller or terminate the repurchase agreement. If the seller defaults, the Fund would suffer a loss to the extent that the proceeds from the sale of the underlying securities were less than the repurchase price. Any such loss would be increased by any cost incurred on disposing of such securities. If bankruptcy proceedings are commenced against the seller under the repurchase agreement, the realization on the collateral may be delayed or limited. Repurchase agreements entered into by the Fund will be limited to transactions with dealers or domestic banks believed to present minimal credit risks, and the Fund will take constructive receipt of all securities underlying repurchase agreements until such agreements expire.

F. The Fund distributes net investment income to shareholders monthly and net capital gains, if any, annually. Distributions from net investment income are determined in accordance with income tax regulations. Dividends from net investment income can exceed the Fund's book basis net investment income. Effective January 1, 1993, the Fund adopted Statement of Position 93-2: "Determination, Disclosure, and Financial Statement Presentation of Income, Capital Gain and Return of Capital Distributions by Investment Companies." As a result, the Fund changed the financial statement classification of distributions to shareholders to better disclose the differences between financial statement amounts available for distribution and amounts distributed to comply with income tax regulations. The significant difference between financial statement amounts available for distribution and distributions made in accordance with income tax regulations is due to the difference in the treatment of 12b-1 Distribution Plan charges.

2. Capital Share Transactions

The Declaration of Trust authorizes the issuance of an unlimited number of shares of beneficial interest with no par value. Transactions in shares of the Fund were as follows:

	Year Ended December 31,	
	1994	1993
Shares sold	16,871,171	20,470,708
Shares redeemed	(43,806,889)	(20,802,266)
Shares issued in reinvestment of: Distributions from investment income-- net and Distributions in excess of investment income--net	5,031,307	5,196,577
Distributions from realized gains--net	0	5,110,384
Net increase	(21,904,411)	9,975,403

The Fund bears some of the costs of selling its shares under a Distribution Plan adopted pursuant to Rule 12b-1 under the Investment Company Act of 1940. The Distribution Plan provides that the Fund may incur certain expenses which may not exceed a maximum amount equal to 0.3125% of the Fund's average daily net assets for any quarter occurring after the inception of the Distribution Plan. Under the Distribution Plan, the Fund pays Keystone Distributors, Inc. ("KDI"), the principal underwriter and a wholly-owned subsidiary of Keystone, amounts which in total may not exceed the Distribution Plan maximum.

In connection with the Distribution Plan and subject to the limitations discussed below, Fund shares are offered for sale at net asset value without any initial sales charge. From the amounts received by KDI in connection with the Distribution Plan, and subject to the limitations discussed below, KDI generally pays brokers or others a commission equal to 3% of the price paid to the Fund for each sale of Fund shares as well as a shareholder service fee at a rate of 0.25% per annum of the net asset value of the shares sold by such brokers or others and remaining outstanding on the books of the Fund for specified periods.

To the extent Fund shares purchased prior to July 8, 1992 are redeemed within four calendar years of original issuance, the Fund may be eligible to receive a deferred sales charge from the investor as partial reimbursement for sales commissions previously paid on those shares. This charge is based on declining rates, which begin at 4.0%, applied to the lesser of the net asset value of shares redeemed or the total cost of such shares.

Since July 8, 1992, contingent deferred sales charges applicable to shares of the fund issued after January 1, 1992 have, to the extent permitted by the NASD Rule, been paid to KDI rather than to the Fund. During the fiscal year ended December 31, 1994, KDI received $745,076 in contingent deferred sales charges.

A rule of the National Association of Securities Dealers, Inc. ("NASD Rule") limits the annual expenditures, which the Fund may incur under the Distribution Plan to 1%, of which 0.75% may be used to pay such distribution expenses and 0.25% may be used to pay shareholder service fees. The NASD Rule also limits the aggregate amount which the Fund may pay for such distribution costs to 6.25% of gross share sales since the inception of the Fund's 12b-1 Distribution Plan, plus interest at the prime rate plus 1% on unpaid amounts thereof (less any contingent deferred sales charges paid by the shareholders to KDI).

KDI intends, but is not obligated, to continue to pay or accrue distribution charges which exceed current annual payments permitted to be received by KDI from the Fund. KDI intends to seek full pay-

ment of such charges from the Fund (together with annual interest thereon at the prime rate plus one percent) at such time in the future as, and to the extent that, payment thereof by the Fund would be within permitted limits. KDI currently intends to seek payment of interest only on such charges paid or accrued by KDI subsequent to January 1, 1992.

During the year ended December 31, 1994, the Fund recovered $97,865 in contingent deferred sales charges. During the year, the Fund paid KDI $13,324,192 under the Distribution Plan. The amount paid by the Fund under its Distribution Plan, net of deferred sales charge, was $13,226,327 (0.97% of the Fund's average daily net assets). During the year, KDI received $9,126,418, after payments of commissions on new sales and service fees to dealers and others of $4,197,774.

3. Securities Transactions

As of December 31, 1994, the Fund had a capital loss carryover for Federal tax purposes of approximately $25,307,000 which expires in 2002. Additionally, the Fund has incurred capital losses of approximately $11,617,000 in the current fiscal year which, under the Tax Reform Act of 1986 are treated for tax purposes as occurring on the first day of the Fund's next fiscal year and are available as an offset to capital gains that may be recognized in the next fiscal year.

For the year ended December 31, 1994, purchases and sales of investment securities were as follows:

	Cost of Purchases	Proceeds from Sales
Tax-exempt investments	$1,103,970,118	$1,229,891,567
Short-term commercial and tax-exempt notes	652,543,980	675,679,000
	$1,756,514,098	$1,905,570,567

4. Investment Management and Transactions with Affiliates

Under the terms of the Investment Management Agreement between KMI and the Fund, dated December 29, 1989, KMI provides investment management and administrative services to the Fund, as well as certain additional operating services, facilities and supplies. In return, KMI is paid monthly, (i) a management fee calculated daily at a rate of 2.0% of the Fund's gross investment income plus an amount determined by applying percentage rates starting at 0.50% and declining as net assets increase, to 0.25% per annum, to the net asset value of the Fund, and (ii) an amount equal to KMI's reimbursable expenses accrued during the year in providing such additional services. KMI has entered into an Investment Advisory Agreement with Keystone, dated December 30, 1989, under which Keystone provides investment advisory and management services to the Fund and receives for its services an annual fee representing 85% of the management fee received by KMI.

During the year ended December 31, 1994, the Fund paid or accrued to KMI investment management and administrative services fees of $7,970,545. Included in this amount is the management fee of $5,941,545, which represented 0.43% of the Fund's average net assets. Of such management fee paid to KMI, $5,050,313 was paid to Keystone for its services to the Fund.

Also included in the total investment management and administrative services fee paid by the Fund were the following approximate amounts incurred by KMI (and reimbursed by the Fund) in providing or obtaining for the Fund the additional operating services, facilities and supplies required by the Agreement: transfer agent fee, $1,418,400; audit and legal fees,

$86,200; custodian fees, $264,100; printing and supplies, $43,100; registration fees, $106,450; and other, $110,750.

During the year ended December 31, 1994, the Fund paid or accrued to KGI $23,917 for certain accounting services and to KIRC $1,418,000 for transfer agent fees. This amount for transfer agent fees is included in the payments made by KMI described in the preceding paragraph.

5. Distributions to Shareholders

The net investment income of the Fund (interest income accrued as earned, less expenses of the Fund) is determined as of the normal close of trading on the New York Stock Exchange each business day on which the exchange is open. The net investment income so determined each day is declared as a dividend to shareholders of record at the time of such determination and is distributed promptly after the end of each calendar month. Any net realized short-term and long- term capital gains in excess of carried-over losses, will be distributed annually. All distributions of net investment income will be paid in cash unless the shareholder has directed that they be reinvested, in which case such reinvestment will be at the net asset value on the last business day of the month in which declared. Any distributions of capital gains will be reinvested in additional shares of the Fund at net asset value on the record date of the month in which declared unless the shareholder has specified that they wish to receive cash. Shares acquired through reinvestment of net investment income or capital gains are not subject to contingent deferred sales charges.

Federal Tax Status--Fiscal 1994
Distributions (Unaudited)

The per-share distributions paid to you for fiscal 1994, whether taken in shares or cash, are as follows:

Income Dividends	
Tax-exempt	Taxable
$0.433	$0.000

In January 1995, complete information on the calendar year 1994 distributions will be forwarded to you to assist you in completing your 1994 federal tax return.