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Mr. Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

10 August 2015

Re: Investment Company Reporting Modernization
(Release No. 33-9776; 34-75002) Commission File No. S7-08-15

Dear Mr. Fields:

Ernst & Young LLP is pleased to comment on the *Investment Company Reporting Modernization* proposal issued by the Securities and Exchange Commission (SEC or the Commission). The proposal would introduce new rules and amend existing rules that govern reporting by registered investment companies (RICs). Among other changes, the Commission proposes amendments to Articles 6 and 12 of Regulation S-X, which prescribe information to be reported in investment company financial statements.

General

The objective of the proposal is to improve the information that funds report to their shareholders and the Commission. We agree that many of these amendments would improve the transparency and comparability of investment company financial statements for their intended users. However, we have concerns about some of these proposals.

In our comments, we have considered whether the proposed amendments would enhance consistency and transparency of financial reporting and whether they achieve the objectives of the Commission's focus on disclosure effectiveness.

Requirement to disclose illiquid securities

The proposal would amend §210.12-12, §210.12-12B, §210.12-13, §210.12-13A, §210.12-13B, §210.12-13C, §210.12-13D and §210.12-14 to include a requirement that investment companies identify each illiquid investment as such. Form N-PORT would define "illiquid asset" as "an asset that cannot be sold or disposed of by the Fund in the ordinary course of business within seven calendar days, at approximately the value ascribed to it by the Fund."

Although we agree with the Commission's intent to provide users of RIC financial statements with information sufficient to enable them to assess the risks associated with a RIC's portfolio investments, we recommend that the Commission defer amending §210.12-12, §210.12-12B, §210.12-13, §210.12-13A, §210.12-13B, §210.12-13C, §210.12-13D and §210.12-14 for the reasons discussed below.

As indicated in the proposing release, the Division of Investment Management is considering a recommendation that the Commission update liquidity standards for open-end funds and exchange-traded funds, which may result in updated guidance on this issue. Our views and comments may change based on any updates, and we encourage the Commission to defer adopting the requirement for RICs to identify each illiquid investment in their financial statements until the liquidity standards have been updated and preparers and users have the opportunity to evaluate and comment on the effects on the proposed amendments.

Furthermore, the criteria to determine whether an asset can be sold or disposed of by the Fund in the ordinary course of business within seven calendar days, at approximately the value ascribed to it by the Fund, have not been defined. Without defined criteria, a lack of comparability is likely.

For example, fixed income securities typically do not trade frequently, and without objective criteria, preparers of RIC financial statements may reasonably reach different conclusions about whether the same security should be deemed illiquid, which would reduce the usefulness of the disclosure to financial statements users. Also, the absence of defined criteria for determining whether an asset is illiquid would impair an auditor's ability to objectively audit management's assertions about whether securities held are illiquid.

Disclosure of notional amounts and value for options and futures contracts

The proposed amendments would require RICs to provide additional disclosures for derivative contracts. Specifically, the proposed amendments would require that the financial statements for RICs disclose the notional amounts for written and purchased options, as well as notional amounts and values for open futures contracts.

We believe derivative disclosures should provide users of the financial statements with information relevant to the risks associated with derivatives. We support requiring disclosures of the notional amounts for open options contracts and notional and value amounts for open futures contracts. However, such requirements should include clear definitions. Without clear definitions, there could be a lack of comparability, and that would reduce the benefit of the disclosures to financial statement users. For example, the value of open futures contracts could be interpreted as cumulative appreciation/depreciation, exchange price multiplied by notional or variation margin receivable/payable. We recommend that the SEC provide clear definitions of the amounts to be disclosed to promote consistent application.

Certain tax basis disclosures expanded to derivatives

Currently, Rule 12-13 of Regulation S-X requires disclosure of the following amounts based on cost for federal income tax purposes as it relates to investments other than securities: aggregate gross unrealized appreciation for all investments in which there is an excess of value over tax cost, aggregate gross unrealized depreciation for all investments in which there is an excess of tax cost over value, the net unrealized appreciation or depreciation, and the aggregate cost of investments. The proposal would extend the requirement of these tax basis disclosures to other rules concerning short sales and derivative holdings, including proposed Rule 12-12A and Rules 12-13 through 12-13D.

ASC 946, *Financial Services — Investment Companies,* requires that investment companies disclose in the notes to the financial statements the components of distributable earnings (i.e., undistributed ordinary income, undistributed long-term capital gains, capital loss carryforwards and unrealized appreciation or depreciation) on a tax basis as of the most recent tax year end.[1] Investment companies also must disclose in the notes to financial statements the tax-basis components of dividends paid (i.e., ordinary income distributions, long-term capital gains distributions and return of capital distributions).[2]

We agree with the Commission that the proposed changes in disclosure requirements would improve consistency in reporting and make investment company financial statements more comparable. However, considering the existing requirements under the Codification, the objective of tax basis disclosures to provide investors with sufficient information to enable them to understand tax characteristics of their investment in an investment company would be achieved by requiring the proposed tax disclosures at the total portfolio level. We believe that disaggregating such information by investment type as proposed could detract from the overall objective of the disclosure requirement.

Securities lending disclosures

The proposal would add subsection (m) to §210.6-03 that would require funds to make certain disclosures with respect to securities lending activities and cash collateral management. Specifically, the proposal would require that funds disclose (1) the gross income from securities lending, including income from cash collateral reinvestment; (2) the dollar amount of all fees and/or compensation paid for securities lending activities and related services; (3) the net income from securities lending activities; (4) the terms governing the compensation of the securities lending agent; (5) the details of any other fees paid directly or indirectly and (6) the monthly average of the value of portfolio securities on loan.

We believe the existing financial presentation, in conjunction with the disclosures already required by ASC 860, *Transfers and Servicing,* paragraph 30-50-1A[3] with respect to securities lending collateral

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1 See ASC 946-20-50-12.

2 See ASC 946-505-50-5.

3 ASC 860-30-50-1A states that:

"An entity shall disclose all of the following for collateral:

a. If the entity has entered into repurchase agreements or securities lending transactions, it shall disclose its policy for requiring collateral or other security.

b. As of the date of the latest statement of financial position presented, both of the following:
   1. The carrying amount and classifications of both of the following:
      i. Any assets pledged as collateral that are not reclassified and separately reported in the statement of financial position in accordance with paragraph 860-30-25-5(a)
      ii. Associated liabilities.
   2. Qualitative information about the relationship(s) between those assets and associated liabilities; for example, if assets are restricted solely to satisfy a specific obligation, a description of the nature of restrictions placed on those assets.

c. If the entity has accepted collateral that it is permitted by contract or custom to sell or repledge, it shall disclose all the following:
   1. The fair value as of the date of each statement of financial position presented of that collateral
   2. The fair value as of the date of each statement of financial position presented of the portion of that collateral that it has sold or repledged
   3. Information about the sources and uses of that collateral.

For overall guidance on Topic 860's disclosures, see Section 860-10-50."

and disclosures already required by Regulation S-X §210.6-04(11) relating to the value of securities loaned and the nature of the collateral received, provides users of financial statements with sufficient information to understand the extent of securities lending activities, associated risks and their effect on RICs.

While we recognize that the requested additional information may be relevant to the Commission's broader effort to improve data collection and analysis, we believe the proposed disclosures would result in the presentation of detailed information with varying degrees of usefulness that could detract from other material information presented in the financial statements. We recommend that the Commission use other reporting mechanisms more suited for that purpose, such as Form N-CEN, rather than requiring this information to be included in RIC financial statements.

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We would be pleased to discuss our comments with the Commission or its staff at your convenience.

Very truly yours,

Ernst & Young LLP