August 16, 2022

Submitted Electronically – rule-comments@sec.gov

Ms. Vanessa Countryman
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: File Number S7-16-22
Proposed Amendments to Investment Company Act Rule 35d-1

Dear Ms. Countryman:

Nationwide appreciates the opportunity to comment on the U.S. Securities and Exchange Commission's (the "Commission") proposed amendments to Rule 35d-1 under the Investment Company Act of 1940, as amended (the "1940 Act") related to investment company names (the "Names Rule"). We agree that a fund's name may communicate a great deal to an investor,[1] and we believe that the Names Rule, in its current form, has been highly effective in ensuring that a fund's name does not misrepresent the fund's investments and risks. We also agree with the Commission's oft-quoted warning that investors should go beyond the name itself and look closely at a fund's underlying disclosures.[2] Nationwide is concerned that many of the amendments to the Names Rule it now proposes (the "Proposed Amendments") would significantly reduce the ability of mutual fund investment advisers, such as Nationwide, to operate the funds they offer in the best interests of their customers. To be clear, we acknowledge the Commission's concerns about the potential for mutual fund names to mislead investors. We nonetheless fear that many of the Proposed Amendments are overly broad, needlessly restrictive, and would interfere with the provision to funds of quality discretionary portfolio management to the detriment of fund shareholders.

We believe that the Names Rule, in its current form, is workable for mutual fund providers primarily because its current focus on types of investments or industries, or countries or geographic regions, is easy to interpret and can be quantified by objective means. Although neither the Names Rule nor Form N-1A formally require a fund to explain in its prospectus how terms covered within the scope of the rule are defined, widespread industry practice, in response to comments from the Commission's disclosure staff, is to use plain English prospectus disclosure to define what such terms mean and how they apply. (e.g., "large-cap stocks are stocks of issuers with market capitalizations within the range of the XYZ

[1] Investment Company Names, Investment Company Act Release No. 34593 (May 25, 2022) [87 FR 36594] (the "Proposing Release"), at 36595.
[2] *Id.*

Index"). Further, the absence of enforcement proceedings or shareholder lawsuits against mutual fund providers attests to the rule's effectiveness in having prevented the use of misleading fund names. In short, with one particular exception, the Names Rule in its current form has successfully met the objectives the Commission sought when the rule was adopted in 2001.

The one exception relates to the increasing number of funds with names that purport to offer some form of an environmental, social or governance ("ESG") strategy. The Commission believes that ESG strategies may be unlike other strategies in that they can consider factors and measures in addition to those often used to measure financial return to manage a portfolio.[3] Nationwide supports the Commission's efforts to develop a common disclosure framework, based on readily available and determinable data, to assist investors in understanding how such strategies operate and the effectiveness in which they meet their goals. Nationwide further recognizes the Commission's concern that certain funds with ESG-oriented terms in their names may exaggerate the degree to which ESG practices inform security selection and portfolio construction. Despite these concerns, the Commission has not found that terms in fund names that suggest other focuses, such as "value" or "growth," have been the subject of abuse. Moreover, the Commission has not demonstrated that shareholders have been misled because a security that met a fund's 80% investment policy at the time it was purchased may, over time, have ceased to so qualify. Nationwide thus recommends that the Commission significantly narrow the scope of the Proposed Amendments to focus more specifically on funds having names that suggest an ESG focus.

About Nationwide Funds Group

Nationwide Funds Group ("NFG") is a mutual fund service provider with a product range distributed through major financial intermediary channels, retirement products and variable annuity and life insurance products. NFG comprises Nationwide Fund Advisors, Nationwide Fund Distributors LLC and Nationwide Fund Management LLC. Together they provide investment advisory, distribution and administration services, respectively, to the Nationwide Funds. NFG is part of Nationwide Financial Services, Inc., which in turn is a wholly owned subsidiary of Nationwide Mutual Insurance Company. NFG is a manager-of-managers, partnering with over 30 subadvisers across 118 different mutual funds and four exchange-traded funds ("ETFs") comprising $87.1 billion in gross assets as of June 30, 2022.

Nationwide's Concerns

Nationwide's comments are oriented around the following three principles:

- With the exception of fund names that include terms suggesting an investment focus on ESG factors, Nationwide opposes expanding the scope of the Names Rule's 80% investment policy requirement to apply to fund names with terms suggesting that the fund focuses on investments that have "particular characteristics;"
- Nationwide opposes amending the Names Rule to change the application of an 80% investment policy from the time of investment, and instead suggests that the Commission's concerns can be adequately addressed through proper disclosure; and

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[3] *See, e.g.,* Enhanced Disclosures by Certain Investment Advisers and Investment Companies about Environmental, Social, and Governance Investment Practices, Investment Company Act Release No. 34594 (May 25, 2022) [87 FR 36654, at 36658].

- Nationwide opposes the Form N-PORT reporting requirements contained in the Proposed Amendments as unduly burdensome and costly but which it sees as unnecessary and likely to do little to protect shareholders.

We discuss each of these issues in greater detail as follows:

1. **Names Suggesting an Investment Focus**

The Names Rule currently requires a fund to adopt an 80% investment policy with respect to words in fund names that indicate an emphasis on types of investments, industries or geographic locations. Much of the success of the Names Rule to date can be attributed to the clarity of this requirement, combined with the flexibility it affords fund managers to define the parameters of terms covered through objective and quantifiable means. Whether a security is an equity or a bond can be discerned based on objective fact. The flexibility the current rule affords enables funds to disclose in their prospectuses what types of companies would be included in a term suggesting a type of investment, industry or a geographic location.[4] Although differences of opinion exist as to what constitutes a small-capitalization company, a prospectus can easily inform investors of what the objective parameters are (based, e.g., on market capitalization, annual earnings, etc.) for purposes of a particular fund. In short, as a piece of regulation the current Names Rule works because its requirements are objective and it communicates to the industry clearly what those requirements are.

The Commission now proposes to include within the scope of the Names Rule terms that can suggest a focus on investments or issuers having "particular characteristics."[5] By itself, the phrase "particular characteristics" is very vague and open-ended, leaving industry participants wondering which words it might encompass. The discussion of this phrase in the Proposing Release and the examples the Commission provides further obscure what "particular characteristics" means because the examples themselves either are highly subjective or otherwise contradict the related discussion. For instance, the Proposing Release explains that "particular characteristics" could be construed to represent either an investment strategy or to connote an investment focus, but is isolated only as to specific investments or issuers, and not to overall portfolio characteristics or any possible result to be achieved.[6] The Commission next indicates that the word "income" would be included within the scope of the Names Rule, because it conveys particular characteristics about specific securities, but the term "real return" (which has a very similar meaning) would not be included. In our experience, the inclusion of the word "income" in a fund's name normally is not meant to suggest investments *having* "particular characteristics" so much as it connotes the *seeking* by a portfolio of a particular outcome.[7] The fact that words such as "income" can mean different things in different contexts only proves the difficulty of expanding the rule to cover "particular characteristics," leaving fund providers wondering what other terms would fall within its scope.

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[4] For example, ". . . a U.S. equity is an equity security of an issuer that (i) is headquartered or domiciled within the United States; or (2) derives at least 50% of its annual revenues from sales or operations in the United States."
[5] Section 35d-1(a)(2) of the Proposed Amendments.
[6] *See, e.g.,* Proposing Release, *supra*, at 36598-36599.
[7] The Commission also indicates that the word "growth" would be included within the scope of the Proposed Amendments, yet a name with the words "growth and income" used together typically is meant to imply an overall portfolio that seeks returns derived from both capital appreciation and dividend or interest income, and not necessarily one that is focused on "growth" stocks.

The Commission also indicates that words such as "growth" or "value," when used in a fund's name, would be covered within the scope of the Proposed Amendments. The fact that these two terms would fall within the scope of the Names Rule is quite clear. Interpreting what these terms mean, however, is not clear because of the subjective nature of how they are defined. Whether a security can be considered to be "growth" or "value" is subject to various interpretations, can depend on market cycles or even be relational to other factors. Some of these interpretations can be defined using objective criteria, while other interpretations require discretionary judgments. Trying to define what is "growth" versus "value" is further complicated by the various types of growth or value strategies that exist.

Some value strategies are defined by lower market prices relative to current earnings, whereas others are defined by lower market prices relative to book value or some other measure. Still other value strategies use contrarian approaches that focus on stocks whose prices are low in relation to current market sentiment, while relative value strategies typically evaluate an issuer's market price primarily in relation to its own past history. Finally, some value strategies identify stocks as value stocks because the portfolio manager simply believes, for whatever reason, that their market prices are below what they should be. Similarly, various types of growth strategies abound, using different criteria to identify growth issuers. Traditional growth typically focuses on issuers whose earnings are growing faster than those of other companies, momentum growth focuses on stocks whose market prices are rising faster than those of other issuers, and quality growth (often known as "growth at a reasonable price") involves identifying companies with earnings or cash flow growth, but with an emphasis on price valuation. Quantitative strategies are typically driven more by quantitative metrics, whereas strategies based on fundamental analysis often rely on the subjective and personal determinations of their portfolio managers. Unlike terms such as "equity" or "bond," which can be discerned based on objective fact, terms such as "value" or "growth" often are applied based on personal opinion.

Certainly many third-party research and index providers categorize stocks by growth or value, but the fact that they do so does not obviate the subjective nature of these terms or the myriad ways that individual issuers can be viewed. Allowing these third-party providers to define such terms transfers the responsibility for making such determinations from portfolio managers and boards of trustees, each subject to fiduciary obligations to fund shareholders, to third-parties having no fiduciary obligations whatsoever. We do not believe that this transfer of responsibility will benefit fund shareholders. We also fear that the subjective nature of the terms "growth" and "value" will result in the imposition of criteria that reflect the individual views of the Commission's staff and not that of portfolio managers, and a second-guessing of which securities ought to be included in a fund's 80% basket by individuals who are not industry professionals. The result of regulatory "pigeon-holing" of securities by strategy types is thus likely to result in fewer strategy variations. Rather than enhance the investor experience, the Proposed Amendments will detract from it by removing the determination of subjective judgments from those who are qualified and hired to make them, and by reducing the number of options in the marketplace.

The Commission furthermore has not demonstrated that shareholders have been misled by funds with terms such as "growth," "value" or "income" in their names. The Commission has, by contrast, articulated the concerns it has with fund names that include ESG-focused terms. Nationwide supports the Commission's efforts to regulate funds proffering ESG strategies but which engage in "greenwashing" or otherwise fail to invest in the manner in which they claim. By specifically tailoring the Proposed Amendments to address its real concern over a distinct type of investment focus, the

Commission can eliminate the vagueness and subjectivity with which the Proposed Amendments are fraught while maintaining the flexibility critical to ensuring differentiation among fund strategies.

2. Temporary Departures from 80% Investment Requirement

Nationwide strongly objects to the Commission's current proposal to modify Rule 35d-1(b) to specify the particular circumstances under which a fund may depart from its 80% investment policy, particularly as it relates to the inclusion of specific time frames for returning to compliance. Any departure from the current requirement -- that an 80% investment policy applies at the time of investment -- would arbitrarily and *unnecessarily* interfere with the ability to effectively manage fund portfolios, to the detriment of our customers who invest in such funds. The adoption of specified time frames for returning funds to compliance with an 80% policy will require funds to sell securities that portfolio managers view as their best performers or would otherwise prefer to hold, thereby impacting investment performance, incurring transaction costs, triggering taxable gains to shareholders and potentially impacting market liquidity.

Our concerns about the Proposed Amendments' potential interference with effective portfolio management cannot be expressed strongly enough. Mutual funds and ETFs are classified as "management companies" under the 1940 Act,[8] the portfolios of which are managed by registered investment advisers under the oversight of boards of trustees. Subject to the authority granted to the investment adviser in an investment advisory agreement that has been approved by the fund's board of trustees (including those trustees that are deemed to be not "interested"), the investment adviser exercises investment discretion, in accordance with its fiduciary duties to the fund and its shareholders, to manage the fund's portfolio pursuant to its investment objective and investment strategies.[9] While Nationwide recognizes that such investment discretion is not absolute, statutory restrictions imposed by the 1940 Act rarely require the divestiture of investments that complied with the regulatory requirements at the time they were purchased. Therefore, a fund that qualifies as a diversified investment company under Section 5(b) of the 1940 Act does not lose its status as diversified because of a subsequent change in the value of the fund's investments.[10] The anti-pyramiding provisions of Section 12(d)(1) do not require a fund to divest its holdings of other investment companies in the event such holdings later exceed the percentage limitations of Section 12(d)(1)(A). These provisions reflect a Congressional preference against forcing the sale of securities that otherwise complied with applicable regulation at the time such securities were acquired. The Commission's rulemaking and interpretive guidance similarly applies typically at the time of purchase or acquisition.[11] These examples evidence a regulatory concern that forcing the sale of securities contrary to the investment adviser's informed judgment can impose arbitrary results on the very investors such regulation seeks to protect.

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[8] 1940 Act Section 4(3).

[9] Section 2(a)(20) of the 1940 Act defines generally defines an "investment adviser" to an investment company to be a person "who pursuant to contract with such company regularly furnishes advice to such company with respect to the desirability of investing in, purchasing or selling securities or other property, or is *empowered to determine what securities or other property shall be purchased or sold by such company . . .*" (emphasis added).

[10] *See* 1940 Act Section 5(c).

[11] For example, the exemptions from Section 12(d)(3) of the 1940 Act provided in Rule 12d3-1 apply at the time of purchase or acquisition; Guide 19 of the 1983 Guidelines for Form N-1A, which formerly were repealed by the Commission in 1998, specified that a fund's concentration policy applied at the time of purchase, and did not require the sale of securities due to subsequent changes in the value of portfolio securities.

Forcing the sale of portfolio securities in order to return to compliance with an 80% investment policy also is unnecessary in order to protect investors from misleading fund names because the Names Rule does not operate in a vacuum. Rather, the Names Rule operates in conjunction with a robust, layered and integrated disclosure regime that advises shareholders of what to expect from their investments. [12] In this regard, Nationwide suggests that the Names Rule can be enhanced to require registrants to disclose clearly in their prospectuses whether a fund's 80% investment policy applies at the time of investment or whether it is a continuing obligation. To the extent an 80% investment policy applies at the time of investment, the Names Rule could be amended to require the inclusion of prospectus language disclosing the risk that the fund's portfolio at times may drift from the types of investments identified in the fund's name due to market forces. Alternatively, if an 80% investment policy is intended to be a continuing requirement, the Names Rule should be amended to require the inclusion of language disclosing the risks of securities divestitures that are made in order to return the fund to compliance with the 80% policy. We point to the current disclosure regime, grounded in the delivery to investors of clear and concise plain English disclosure in summary form, and supplemented by layers providing additional degrees of detailed information, as working very effectively in informing investors about funds' investments, strategies and risks. We believe that the Name Rule works best *in conjunction with* the Commission's disclosure regime, not in lieu of it.

3. <u>N-PORT Requirements</u>

Nationwide opposes the inclusion of new N-PORT reporting requirements in the Proposed Amendments for two reasons. First, most of the new requirements relate to departures from a fund's 80% investment policy and the length of time thereof. Because Nationwide believes that any 80% investment policy mandated by the Names Rule should apply only at the time of investment, any reporting related to departures from such investment policies is unnecessary.

Even were the Commission to proceed with new N-PORT reporting requirements, Nationwide questions the wisdom and practicality of any such new requirement. Nationwide challenges the Commission's assertion that the N-PORT reporting requirements would provide investors with important information regarding how a fund implements an investment focus.[13] We are of the view that a fund's prospectus, particularly the summary statement of its strategies and risks in response to Form N-1A Item 4, is significantly more comprehensible to investors and is more likely to be read than are N-PORT filings.

We do agree that N-PORT reporting would provide the Commission staff with increased transparency, and would enhance the Commission's ability effectively to oversee and assess funds' activities. Nationwide does not oppose, in principal, providing the Commission staff with greater tools to protect investors, but only does so in this case due to the increased costs to mutual funds and amplified burdens on fund administration and compliance personnel that would result, particularly given that the Commission has not demonstrated widespread abuse under the Names Rule in its current form (with the exception of ESG-focused funds), nor has it demonstrated that mutual fund and ETF investors currently are being harmed by misleading fund names. We are concerned about increasing the demands on critical and already limited compliance personnel, particularly with the adoption of

[12] Investors who choose not to read the disclosures should not be excused from their own responsibility to do so, especially as the average length of a summary prospectus is four pages long. The Commission has often cautioned against investors relying on a fund's name as the sole source of information about its investments and risks. *See Proposing Release, supra,* at 36595.
[13] Proposing Release, *supra,* at 36617.

comprehensive new regulatory requirements in recent years,[14] and fear diverting the attention of such personnel from more compelling compliance concerns, such as investing in impermissible securities, unlawful transactions with affiliates, front-running transactions by access persons or marketing or sales practice violations.

Conclusion

The Names Rule is an important tool in protecting investment company investors from deceptive or misleading fund names, but it was never contemplated as a substitute for clear and complete prospectus disclosure. We acknowledge the Commission's interest in addressing concerns about greenwashing. Nevertheless, we also believe the broad and sweeping approach taken in the Proposed Amendments would frustrate the Commission's stated goals and policy concerns to the detriment of mutual fund shareholders. Nationwide instead recommends modifying the Proposed Amendments as described herein to more narrowly address the unique circumstances of ESG investing.

We look forward to discussing these issues with the Commission, and we hope the Commission will accept that these comments are informed by our real-world experience in managing mutual funds and ETFs for the benefit of Americans who are preparing for or living in retirement. Our commitment to our customers has been the bedrock of our company since the beginning, and we appreciate the chance to offer our views on this important regulatory proposal.

Please contact Carson Lewis in our Government Relations Department at 202-347-9591 or via email at [redacted] for any follow up questions you may have.

Sincerely,

Michael S. Spangler
President and Chief Executive Officer
Nationwide Funds Group

[14] *See, e.g.,* Rule 22e-4, requiring funds to adopt and maintain liquidity risk management programs, and Rule 18f-4, requiring funds that use derivatives to adopt derivatives risk management programs for funds that do not qualify as limited derivatives users.