Dechert LLP

1900 K Street, NW
Washington, DC 20006-1110
+1 202 261 3300 Main
+1 202 261 3333 Fax
www.dechert.com

August 16, 2022

VIA ELECTRONIC DELIVERY

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

Re: Investment Company Names (File No. S7-16-22)

Dear Ms. Countryman:

We appreciate the opportunity to respond to the request by the U.S. Securities and Exchange Commission ("SEC" or "Commission") for comments regarding the above-referenced release (the "Release"). In the Release, the SEC proposed amendments to Rule 35d-1 (the "Names Rule") under the Investment Company Act of 1940 (the "Investment Company Act") and several related forms.[1] The proposed amendments would expand the requirement for certain funds[2] to adopt a policy to invest at least 80% of their assets in accordance with the investment focus that the fund's name suggests and, among other items, would establish a new approach to compliance with a fund's 80% investment policy, establish new requirements surrounding the treatment of derivatives in connection with a fund's 80% investment policy, establish new recordkeeping requirements, and introduce additional prospectus disclosure and Form N-PORT reporting requirements.

Dechert LLP is an international law firm with a wide-ranging financial services practice that serves clients in the United States and abroad. In the United States, we represent a substantial number of U.S. mutual fund complexes, closed-end funds, exchange-traded funds, business development companies, fund boards, fund independent directors, fund advisers and fund service providers. In developing these comments, we have drawn on our extensive experience in the financial services industry generally. Although we have discussed certain matters addressed in the Release with some of our clients, the comments that follow reflect only the views of a group of attorneys in our financial services practice, and do not necessarily reflect the views of our clients, other members of our financial services group or the firm generally.

We acknowledge the care and effort the Commission has put into preparing the Release. However, we have significant concerns regarding a number of aspects of the proposal. As discussed in greater detail herein, we believe that:

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1 *See* Investment Company Names, SEC Release No. IC-34593 (May 25, 2022), available at https://www.sec.gov/rules/proposed/2022/ic-34593.pdf ("Release").

2 As used in this letter, the term "fund" refers to registered investment companies and business development companies ("BDCs").

- The Commission has not demonstrated a need for the proposed changes, particularly in light of other outstanding Commission proposals addressing fund disclosure practices.

- A number of the proposed changes, if adopted, would result in significant interpretive issues, impose considerable costs on funds and unnecessarily limit the ability of professional portfolio managers to make investment decisions that are in the best interest of funds and consistent with the funds' disclosed investment objectives and strategies. These include:

  - the proposed expansion in the scope of the Names Rule to include terms such as "growth," "value," "income," "global" and environmental, social and governance ("ESG")-related terms;

  - the replacement of the Names Rule's existing time-of-acquisition test with an ongoing compliance requirement;

  - the Release's guidance on the application of the Names Rule to index funds; and

  - the new recordkeeping and Form N-PORT disclosure requirements.

- The proposed compliance timeline is far too short in light of the considerable compliance burdens that funds would experience as a result of the proposal.

- The Commission's analysis of the costs and benefits of the proposal does not adequately reflect the true burden that implementation of and compliance with the proposed amendments to the Names Rule would impose on funds and their investment advisers.

Thus, although we generally support the Commission's objective of improving and clarifying the Names Rule, we are deeply concerned that the proposal would not achieve the goals of better informing investors or reducing the scope of interpretive issues that arise under the rule. While we have suggested, throughout our comments, ways to improve the amendments if adopted, we believe that the scope of the revisions required and the need for additional guidance to avoid significant uncertainty concerning the Names Rule favor reproposing the amendments prior to adopting a final rule.

I. Expanding the Scope of the Rule is Unjustified and Risks Harm to Investors

A. Expansion to Cover "Particular Characteristics"

1. The Proposed Expansion

The proposed amendments would dramatically expand the 80% investment policy requirement to cover any names suggesting that a fund focuses on investments that have, or whose issuers have, particular "characteristics."[3] The proposal offers little in the way of elaboration concerning what constitutes a "characteristic," with no definition in the proposed amendments or in the Release. Instead, the proposed amendments provide only that this expanded standard would encompass, among other terms, "growth,"

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[3] Release at 19.

"value," and "terms indicating that a fund's investment decisions incorporate one or more ESG factors."[4] To this short list the Release adds a handful of additional terms, including "income," "global," "international," and "intermediate term (or similar) bond."[5]

2. The Proposed Expansion Creates Interpretive Issues

The proposed expansion in the scope of the Names Rule raises numerous interpretive issues. These include, for example:

- The amendments would leave unclear what terms would be deemed to suggest a focus in investments that have, or whose issuers have, particular characteristics. As noted above, the proposed rule and the Release provide little guidance, leaving funds, advisers, counsel and the Commission staff with the task of sorting out the details through the comment process, a result that the proposal seems intended to avoid.

- For the same reason, where a fund has adopted an 80% investment policy tied to particular characteristics, the proposed amendments would be difficult to apply. In this circumstance, there would be significant questions regarding whether a given investment is consistent with that policy.

- Unlike the categories that the Names Rule currently covers, the proposal includes terms that are inherently subjective and do not lend themselves to quantitative, asset-based tests. As a result, they create challenges for compliance while adding little to the general principle that names must not be misleading.

- The limited guidance that the proposal provides applies confusing, disparate approaches to similar concepts. For example, the Release states that the 80% investment policy requirements would not apply to terms—such as "duration"—that describe "characteristics of a fund's portfolio as a whole."[6] At the same time, the Release also indicates that similar terms historically recognized as connoting characteristics of a fund's overall portfolio (such as "intermediate term bond") would implicate the Names Rule under the proposed amendments.

- While the Release clarifies that terms that indicate a particular result or outcome that a fund seeks to achieve do not suggest a focus on investments that have particular characteristics, the distinction is inherently unclear with respect to many terms.[7] For example, certain terms—such as "growth" or "income"—could refer either to a particular portfolio investment or to the overall objective that a fund seeks to achieve. Furthermore, the Release seems to indicate that terms such as these must be read to refer only to the particular portfolio investment, regardless of whether the fund has prominent disclosure indicating the intended meaning of the term, which is inconsistent with longstanding industry usage and unduly restrictive.[8]

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4 *Id*.

5 *Id.* at 24.

6 *Id*.

7 *Id.* at 25.

8 Release at n. 49.

- Terms like "growth" and "value," for example, are fluid concepts that may be subject to qualitative judgments based on criteria that can vary both among sources and over time. In this regard, a single issuer may, under reasonable alternative definitions, be regarded as both a growth and a value company simultaneously, and different portfolio managers may reasonably use different definitions to evaluate issuers. This challenge is only compounded when a fund uses a multi-manager structure or invests in other funds, because the judgements of different managers may, reasonably, vary.

These issues are fundamental to the proposed expansion in scope and not susceptible to resolution through additional guidance in an adopting release. In other words, while the Commission could specify more terms that are or are not "particular characteristics," an exhaustive list is infeasible and likely to become outdated before the Commission revisits the rule again. In suggesting that nearly any descriptive word that could appear in a fund's name must be reducible to a quantitative test, the proposed amendments simply demand too much of individual terms. As a result, the proposed amendments risk either depriving investors of useful information or constraining management of a fund based on information that is designed to be useful, not comprehensive.

3. The Proposed Expansion Will Limit Innovation

Funds that pursue thematic investment strategies, such as funds that focus on infrastructure, blockchain technology or electric and automated vehicles, will face particular challenges. These funds may pursue their strategies in a variety of ways, potentially capturing the entire value chain associated with a particular theme, spanning a wide range of industries and geographies. As a result, such a fund's investments may vary widely in terms of industry, capitalization range, asset class and other key characteristics. Requiring an 80% investment policy based on particular characteristics will either compel such a fund to use a generic name or potentially deprive investors of access to an innovative strategy because the range of investments cannot be reduced easily to a quantitative test.

The Release provides that a fund may define terms used in its name "in a reasonable way" and acknowledges that there may be numerous valid "reasonable" formulations for a particular term or name.[9] In this regard, the Release indicates that, with respect to a name suggesting an investment focus in a particular industry, the Commission would view as a reasonable definition any "securities issued by companies that derive more than 50% of their revenue or income from, or own significant assets in, the industry."[10] While such a definition could be administrable in the case of names that align with well-defined industries, a fund whose name indicates a thematic investment strategy may have difficulty satisfying such a test or may be forced to exclude companies that are nevertheless consistent with the fund's investment theme. For example, such a test could prevent investors from gaining exposure to existing, established companies that are expanding into a new, innovative sector of the market and which may not distinguish such revenue streams from those associated with their core business lines or new companies that have yet to earn income.

Further, according to the Release, the Commission does not believe that the use of "text analytics" or "natural language process" alone is appropriate to evaluate whether a company is sufficiently tied to a

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[9] Release at 26-27, 79.

[10] *Id.* at 27.

particular "theme."[11] However, other than the 50% revenue test noted above, the Release does not provide guidance as to what other tests the Commission would deem to be reasonable, nor does it identify the criteria it would consider in evaluating whether a particular definition is reasonable. Instead, as with the "particular characteristics" concept discussed above, the Commission has merely provided scant examples and left it to each fund to interpret the requirement, thereby inviting inconsistent application and second-guessing. Rather than reducing interpretive issues, the inclusion of these strategies in an 80% investment policy only seems to add difficult and new interpretive issues for investors, funds and Commission staff.

4. The Proposed Expansion Is Unjustified

For the reasons discussed above, we disagree with the proposed expansion of the Names Rule to include names suggesting investments with particular "characteristics." We do not believe that the Commission has articulated or demonstrated a compelling justification for expanding the 80% investment policy requirement to encompass such terms. Notably, the Commission does not point to evidence of investor harm resulting from current market practice with regard to fund names or any lack of efficacy or compliance with the existing Names Rule. In addition, investors have access to numerous sources of information beyond a fund's name that can provide them with a more comprehensive view of the fund. These include, among other things, a fund's prospectus and shareholder reports, information about the fund's portfolio holdings and the historical performance of the fund (individually and as compared to market indices).

At the same time, we believe this change will result in costs to investors resulting from the unnecessary complexity and inevitable confusing and inconsistent application of the 80% investment policy requirement across the industry, as well as costs to funds and advisers, which will be subject to the compliance risks associated with a vague legal standard. The proposed expansion of the 80% investment policy requirement would significantly increase funds' compliance burdens and divert resources from other important compliance matters. Developing and applying compliance testing aimed at capturing subjective characteristics, including cases where those characteristics may vary between funds and portfolio managers, would be highly challenging and time consuming and would require redirecting portfolio managers' focus and attention away from implementing a fund's investment strategies and seeking to maximize returns for investors.

We also have concerns that this proposed expansion of the 80% investment policy requirement could lead to broader use of more generic fund names that convey less information to investors. The proposed amendments also could incentivize the adoption of longer, more complex names that seek to capture the full range of investments reflected in a fund's investment strategy.

This proposed expansion also could have an anti-competitive impact on the fund industry by encouraging homogenization and chilling creative and innovative strategies in actively managed funds, while also limiting the range of acceptable indices that a passively managed fund may track (as discussed below). Ultimately, such a trend could result in investors having fewer meaningful choices. We do not think this is an intended consequence, but it is a risk that must be considered by the Commission.

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[11] *Id.*

5. Alternative Approaches

When the Commission adopted the Names Rule, it recognized that an "investment company's name, like any other single piece of information about an investment, cannot tell the whole story about the investment company."[12] While the Commission has, in the proposed amendments, made an admirable attempt to draw lines that can be applied universally, it simply is not feasible to reduce the nuanced decisions that are required to manage a fund to a single piece of information. To the contrary, investment strategy and risk disclosures are the appropriate vehicle for communicating nuanced strategy characteristics to investors. In this regard, we note that investors who wish to obtain information about a fund and its holdings have at their fingertips access to more information than at any time in history, including on funds' websites and through third-party channels, such as retirement and brokerage platforms. We believe the Names Rule in its current form is effective *because* of, and not in spite of, the fact that its 80% investment policy requirement is limited to a well-defined set of terms that are capable of being objectively measured.

If the Commission determines to adopt expansions to the scope of the Names Rule, we respectfully request that the Commission consider the following alternatives:

- More narrowly tailor the proposed expansion to cover only those terms that may be readily reduced to concrete, objective and measurable characteristics and for which evaluations, opinions and views may not reasonably vary.

- If the Commission determines to apply the Names Rule to terms such as "growth" and "income," it should recognize that these terms may refer *either* to characteristics of a fund's individual investments or to the intended result of the portfolio as a whole and, accordingly, should not categorically include such terms in the scope of the 80% investment policy requirement.

- Provide clear guidance as to how a fund would determine whether a term implicates the expanded Names Rule to reduce uncertainty and inconsistent application of the rule across the industry.

B. The Inclusion of "Global" and "International" in the Scope of the Names Rule Is Inappropriate and Would Continue to Give Rise to Interpretive Uncertainty

1. The Proposed Expansion

The Release states that the proposed expansion of the 80% investment policy requirement under the Names Rule would encompass the terms "global" and "international." While the Commission historically has not required a fund using one of those terms in its name to adopt an 80% investment policy for such terms,[13] the Commission's disclosure review staff has historically commented on the use of "global" and "international" in a fund's name and required funds to adopt certain investment policies tied to those terms.

2. The Proposed Expansion Creates Interpretive Issues

The proposed expansion will create interpretive issues because, in many cases, these policies (*e.g.*, investing in issuers in a minimum number of different countries) are not capable of being formulated as an 80%

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12 Investment Company Names, Release No. IC-24828 (January 17, 2001) at Section I ("Adopting Release").

13 *See id.* at n. 42 and accompanying text.

investment policy, as required by the text of the rule. As the Commission correctly observed in the Adopting Release, when it excluded these terms from the Names Rule, the "[t]he terms 'international' and 'global' […] connote diversification among investments in a number of different countries *throughout* the world."[14] Notably, the Commission and the staff's reasoning at the time was not tied to the distinction between names connoting a type of investment and names connoting an investment strategy (unlike with respect to certain other terms historically excluded from the scope of the Names Rule). Rather, the exclusion of these terms from the Names Rule derives from the fundamental universality of these terms.[15] The application of an 80% investment policy only makes sense when there is a possibility that some investments will fall outside the universe defined by the policy. That is, for such a test to be meaningful, it must contemplate the potential *exclusion* of some investments. Indeed, we are unable to identify a single investment that could not reasonably be treated as part of a "global" or an "international" investment portfolio.[16]

3. Alternative Approaches

We respectfully recommend that the Commission not adopt this expansion. The Commission should recognize that while the Names Rule's 80% investment policy requirement may be a suitable tool for addressing certain terms (*i.e.*, those covered by the existing Names Rule), it is not a panacea for addressing potential misleading naming conventions and, indeed, is wholly inapposite in certain contexts. This is not to say that a fund whose name contains the term "global" or "international" is incapable of having a portfolio that renders its name misleading. Indeed, such terms certainly imply a degree of geographical diversification. Such a fund might, for example, be viewed as having a misleading or deceptive name if, in the ordinary course, it invested substantially all of its assets in issuers in a single country (particularly if that country were the United States). The Commission should acknowledge, however, that such considerations are properly evaluated by reference to the reasonable expectations of investors.

In the alternative, if the Commission determines to adopt this expansion, we encourage it to affirm that the historical staff positions on these terms could serve as a basis for seeking to design a "reasonable" 80% investment policy under the proposed amendments.

C. Short-, Intermediate-, and Long-Term (or Similar) Terms used in Bond Fund Names Should Not Implicate the Names Rule

1. The Proposed Expansion

The proposal would change the treatment of short-, intermediate-, and long-term bond funds under the Names Rule.[17] Historically, the staff of the Division of Investment Management has taken the position that

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[14] *Id.* at n. 42 (emphasis in original). *See also* Frequently Asked Questions about Rule 35d-1 (Investment Company Names) (the "Names Rule FAQ") ("The terms 'international' and 'global' connote diversification among investments in a number of different countries throughout the world, and *therefore* the use of these terms in a fund name is not subject to the rule" (emphasis added)).

[15] *See id*.

[16] For these reasons, the proposed inclusion of terms such as "international" and "global" is also incompatible with the Commission's proposed Form N-PORT reporting requirements because a fund would be unable to meaningfully characterize particular securities as either within or outside of any 80% investment policy tied to these terms.

[17] Release at 24.

the Names Rule does not require an 80% investment policy for funds whose names include "intermediate-term" or similar names because, as the staff accurately recognizes, "intermediate term bond" or similar such terms are meant (and understood) to be a characteristic of a fund's portfolio as a whole.[18] In light of this, the staff has historically required such funds to have an appropriate dollar-weighted average maturity, measured at the portfolio level, rather than employing an 80% investment policy for each portfolio investment.[19]

2. The Proposed Expansion Is Unjustified

We believe that, following two decades of practice adopted in response to staff guidance, investors understand how these terms are used in fund names. We recognize that there is a technical distinction between duration (which is the measurement of certain characteristics of a portfolio of assets) and maturity (which describes the remaining term of a particular debt instrument and is one component of calculating a portfolio's duration). We believe, however, that investors understand the terms "short-," "intermediate-," and "long-term" and similar terms to refer generally to the average time to maturity of a fund's overall portfolio. Investors reasonably rely on the expertise of investment advisers to construct a portfolio reflecting the indicated maturity profile in pursuit of achieving a fund's investment objectives in a manner consistent with its investment strategies and policies. This approach aligns with the time-tested position articulated by the staff in 2001 and, consequently, reflected in the experience of shareholders over the past 21 years. Requiring these funds to adopt an 80% investment policy would necessitate significant changes in the portfolios of certain funds without any measurable benefit or improvement in clarity for investors. In light of this, we believe that the status quo treatment of funds with such names is consistent with investor expectations and not misleading. To the contrary, given the expectations that have been established by the staff's longstanding positions, any change would be inconsistent with these terms' "established industry use."[20] Accordingly, we oppose the proposal to include these terms in the scope of the Names Rule and, instead, encourage the Commission to affirm the staff's historical approach.

II. Prescriptive New Requirements Linked to the 80% Investment Policy Risk Harm to Investors

A. The Proposed Amendments

Currently, the Names Rule requires a fund to comply with its 80% investment policy "under normal circumstances"[21] and measures compliance using a time-of-acquisition test.[22] The Commission has proposed to permit a fund to deviate from its 80% investment policy only in certain enumerated circumstances.[23] In addition, the amendments would require a fund to return to compliance with its 80%

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[18] Names Rule FAQ at Questions 11 and 12.

[19] *Id.*

[20] *See* Release at 199.

[21] 17 C.F.R. § 270.35d-1.

[22] *Id.*; Release at 38-39.

[23] *See* Release at 33-34.

investment policy as soon as reasonably practicable and, in any event, within 30 days, with limited, specified exceptions.[24]

1. The Proposed Amendments Would Operate to the Detriment of Funds and Their Shareholders

The proposed amendments represent a dramatic change from the current Names Rule and would risk constraining management of a fund precisely under the circumstances when discretion may be essential. As a result, the proposed amendments would operate to the detriment of funds and their shareholders, including for the following reasons:

- The proposed amendments would impose mechanical constraints on portfolio management that are fixed in advance and applied on an ongoing basis. However, the Commission and market participants know all too well that it is impossible to predict in advance every circumstance that could make a temporary departure from a fund's 80% investment policy appropriate. A fund's inability to respond appropriately to such unforeseeable circumstances could harm the fund and its shareholders.

- As a result of the proposed continuous testing regime, a fund may be forced to sell securities at undesirable prices and inappropriate times. Such transactions could generate unwanted capital gains, increase transaction costs, reduce diversification and impose longer-term negative consequences on a portfolio. This could occur, for example, when an issuer in a fund's portfolio grows successfully, such as when a small-cap issuer becomes a mid-cap issuer.

- Similarly, the proposed amendments could force a fund to sell holdings in the context of severe market dislocations. While the proposed amendments permit deviations in response to market fluctuations or to take a position in cash or cash equivalents or government securities to avoid losses in response to adverse market, economic, political or other conditions,[25] a fund would be required to return to compliance as soon as reasonably practicable and in any case within 30 days.[26] Market dislocations have, unfortunately, lasted more than 30 days, and because every disruption, crisis and adverse condition is unique, a prescriptive rule risks exacerbating the potential for these events to adversely affect investors.

- In addition, forced sales could expose funds to front running. The programmatic operation of the proposed amendments could enable other investors to anticipate a fund's need to sell securities by analyzing publicly available holdings data and opportunistically taking advantage of funds required to engage in such forced sales.

- Beyond affecting individual funds, under certain market conditions, many funds with similar 80% investment policies could be forced to act simultaneously. Such forced sales could serve to further intensify the market conditions that prompted the dislocation in the first instance.

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[24] *Id*.

[25] Release at 33-34. The Release also permits a fund to temporarily depart from its 80% investment policy to address unusually large redemptions, which could accompany market turbulence. *Id*.

[26] Release at 34.

- Finally, the proposed amendments could actually confuse investors when strategies are intended to specifically contemplate management discretion to address market changes and events.

When the Commission adopted the current Names Rule, it recognized the risk of forced sales, stating that funds should not be required to "sell portfolio holdings that have increased in value" in order to reattain compliance with their 80% investment policies.[27] The proposed amendments, however, would reverse course, requiring that a fund's name drive its investment strategy by requiring it to divest securities that the portfolio manager may otherwise have continued to hold and that are not inconsistent with the fund's investment strategy and the course of action that the portfolio manager believes to be the most appropriate for the fund. This proposal represents a dramatic, and potentially disruptive, change in approach, and the Release does not present evidence or data to justify such a departure or sufficiently weigh the potential adverse effects.

Moreover, the proposed amendments would prevent investors from having access to funds that both (1) are actively managed in ways that enable them to weather prolonged crises or market disruptions through adjustments to their portfolios and (2) have a name that meaningfully reflects the fund's investments (*i.e.*, a name subject to an 80% investment policy). For example, a fund having "small-cap" in its name could not pursue a strategy that provides management with flexibility to invest significantly in other securities or cash during significant market dislocations or crises or during times when the portfolio managers are not able to find sufficient attractive investment opportunities. This aspect of the proposal is striking because, under the revised rule, a fund could not pursue such a strategy regardless of the type or amount of disclosure it provides. In other words, the Names Rule would give individual words in the name of a fund primacy over any other information provided to investors. This would reduce investor choice and unduly limit active managers' ability to exercise judgment.

2. The Proposed Amendments Would Impose Unjustified Costs

We believe the proposed amendments would impose significant, and unjustified, burdens on funds and fund sponsors. While the Release claims that the proposed amendments would address the risk that funds might "drift" from their 80% investment policies,[28] the current framework already imposes effective limits on "drift," as the Release acknowledges. In particular, the existing Names Rule requires that "future investments must be made in a manner that will bring the [f]und into compliance" if a fund is out of compliance with its 80% investment policy.[29] Accordingly, the current framework already provides an effective check on a fund's ability to deviate from its 80% investment policy.

In addition, without justifying the need for a change, the Commission has proposed to require funds to test their portfolios each day for any passive breaches of the funds' 80% investment policy. Such a requirement would impose substantial burdens on funds, their sponsors and their administrators. Such ongoing testing would be even more challenging in the case of certain of the highly subjective terms that the proposed amendments would absorb into the scope of the Names Rule, given that such terms, as discussed above, are not readily quantifiable.

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[27] Adopting Release at n. 32.

[28] Release at 14-15.

[29] 17 C.F.R. § 270.35d-1(b).

3. Alternative Approaches

For the reasons discussed above, we believe the Commission should preserve both the "under normal circumstances" standard and the "at the time of investment" compliance standard. Together with the existing prohibition on materially deceptive or misleading names in Section 35(d) of the Investment Company Act, these standards have proven workable and effective. In particular, the current standards balance the reasonable expectations that arise from a fund's name with the flexibility necessary for managers to exercise discretion when a departure is in the best interests of the fund. The proposal would upend this balance, transforming a fund's name from a useful, but limited, means of communicating with investors into a substitute for judgment. Moreover, these restrictions will have their greatest effect precisely under those circumstances when judgment is most essential.

Moreover, the existing time of investment standard is consistent with other portfolio compliance tests under the Investment Company Act. The diversification and industry concentration provisions in Section 5, the anti-pyramiding provisions of Section 12(d)(1) and the limitations on investments in securities-related issuers in Section 12(d)(3) are all measured on a time-of-acquisition basis.[30] A departure from this approach would be both harmful and burdensome.

If the Commission determines to adopt amendments to the existing standards, we respectfully recommend that it provide for greater flexibility for managers to adjust a fund's portfolio holdings in response to times of crisis or other appropriate situations. There are numerous alternatives that we believe would be less harmful to funds and their investors and less burdensome than those proposed by the Commission. These include, for example:

- The Commission could require board communication under certain circumstances. A fund that falls out of compliance with its 80% investment policy for more than 60 days, for example, could be required to notify its board of the departure and to present a plan to come back into compliance with the 80% investment policy (or to make changes to the fund's name or policy) in a manner that is in the best interests of the fund and its shareholders, which could occur over an extended period, particularly in times of market stress. Adopting this approach would parallel aspects of the framework established under Rule 22e-4 under the Investment Company Act, for example.[31] If such an approach is appropriate in the case of managing portfolio liquidity, then it should also be a reasonable way to address departures from a fund's 80% investment policy under the Names Rule.

- If the proposal is not otherwise revised, the Commission should, at a minimum, recognize certain terms in a fund's name that would signal to investors that the fund is permitted flexibility consistent with the current rule. For example, a fund's name could include the word "managed" (*e.g.*, the

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[30] *See* 15 U.S.C. §§ 80a-5 and 80a-12. Similarly, the leverage limitations in Section 18 of the Investment Company Act are measured at the time a senior security is issued by a fund. *Id.* at § 80a-18.

[31] Under Rule 22e-4, the fund's liquidity program administrator must notify a fund's board if the fund holds more than 15% of its net assets in illiquid investments that are assets and present the board with a plan to bring the fund's illiquid investments that are assets to or below 15% of fund net assets within a reasonable period of time. *See* 17 C.F.R. § 270.22e-4(b)(1)(iv)(A). Similarly, if the fund experiences a shortfall of the fund's highly liquid investment minimum lasting more than 7 consecutive calendar days, the fund's liquidity program administrator must report to the board with an explanation of how the fund plans to restore its minimum within a reasonable period of time. *Id.* at § 270.22e-4(b)(1)(iii)(A)(*3*).

"Managed Large-Cap Growth Fund") to signal that it could depart from its 80% investment policy in a manner consistent with the current Names Rule's "under normal circumstances" standard. This would provide investors with the option to choose the level of discretion they wish to assign to a fund's manager.

- The Commission should expand the scope of acceptable temporary departures to include, at a minimum: (1) the repositioning of fund assets in connection with changes of sub-advisers or portfolio managers; (2) the period leading up to a material investment strategy change; and (3) in connection with the addition or removal of a co-subadviser.

III. Guidance Related to Compliance with an 80% Investment Policy Raises Additional Concerns

A. Guidance Related to Index Funds Would Impose Inappropriate Oversight Responsibilities

The Release includes worrisome new statements about the relationship between an index fund's name and the components of the underlying index. We are concerned that these statements may be read to impose new, and inappropriate, oversight responsibilities on funds. Specifically, the Release states that, even though an index fund may be appropriately invested in its disclosed index, the "underlying index may have components that are contradictory to the index's name" and that under such circumstances, the fund's name may be materially deceptive or misleading.[32] We are concerned that these statements could be read to impose on a fund's investment adviser an unwarranted and inappropriate degree of oversight or supervision of index providers. In addition, because of the wording in the Release, we are concerned that these expectations may extend not only to funds with names including the word "index" but also to any funds that have adopted 80% investment policies that are defined by reference to an index.

While fund sponsors conduct initial and ongoing periodic due diligence on index providers, index funds rely upon the index providers, on a daily basis, to construct the index. Funds make clear disclosures concerning their use of indices, and we believe investors have established a clear understanding of how index funds operate in the decades since their introduction. The guidance in the Release seems to disregard these established practices and, without justification, would impose significant increased burdens on investment advisers. In particular, although we believe this may have been unintentional, the Release's guidance could be interpreted to impose on investment advisers an obligation to closely and continuously scrutinize the operations of unaffiliated index providers, undermining decades of market practice and investor expectations concerning passive management. An index fund should not be required to perform a daily compliance test with respect to whether an underlying index has components that could be perceived to be, or to have become, contradictory to the index's name.

To the extent the guidance is applied to require funds to invest in securities departing from the constituents of the index, this guidance could also result in increased tracking error, frustrating the goals of investors who purchase index funds anticipating exposure that reflects the underlying index. The requirement also may place a fund in the untenable position where it would need to choose between following its replication/sampling strategy or violating the Names Rule or its 80% investment policy.

These problems become more significant in the period prior to a rebalancing. Specifically, the guidance could be read to indicate that a fund has a materially deceptive name during a period prior to a rebalancing

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[32] Release at 70.

of the index if more than 20% of the assets making up the index are replaced in the rebalancing.[33] It may be impossible for an adviser to determine the moment when more than 20% of an index no longer meets the criteria for initial inclusion in the index or has become "contradictory" to the index's name.

Shareholders who have chosen to invest in an index fund expect that the fund will seek to perform like the index, rather than performing like what the adviser believes the composition of the index should be based on a name. Indeed, for an index fund, departing from a strategy of investing to track the index may, itself, be materially misleading.

As a result, we strongly oppose the guidance concerning the Names Rule's treatment of index funds and believe the Commission should disaffirm it at adoption. Alternatively, we request that the Commission confirm that an index fund complies with its 80% investment policy and does not otherwise have a materially misleading name if it tracks an index that has an index construction methodology that is consistent with its name.

B. Guidance Related to "Antithetical" Investments Is Overbroad

The Release includes statements relating to a fund holding investments that are "antithetical" to its investment focus and a fund that "invests in a way such that the source of a substantial portion of the fund's risk or returns is different from that which an investor reasonably would expect based on the fund's name."[34] We are deeply concerned that, unless the Commission rescinds the guidance or offers considerably better clarity, these statements could result in broad readings and interpretive issues. In particular, the guidance provided in the Release is so vague that it may, as a practical matter, replace the 80% standard with a 100% standard. The term "antithetical" is highly subjective, inviting differences of opinion to drive the application of a significant and restrictive rule. Moreover, it is unclear how the term "antithetical" relates to, illuminates or improves compliance with a law that already forbids "misleading" names.

While we believe the Commission should disaffirm this guidance at adoption, if the Commission does adopt a form of this guidance, it should clearly define the contours of what it would view as misleading under this framework. For example, the Commission should, at a minimum, make clear that an investment that is merely inconsistent with a fund's 80% investment policy would not rise to the level of being antithetical.[35]

C. Addressing ESG in the Names Rule is Premature

On the same day that the Commission proposed amendments to the Names Rule, it also proposed to amend certain rules and forms under the Investment Company Act and the Investment Advisers Act of 1940 to

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[33] This interpretation would be somewhat contradictory to a statement in the Release that such a rebalancing could result in a justified temporary departure from a fund's 80% investment policy that would need to be addressed as soon as reasonably practicable, but in no event longer than 30 days. *Id.* at 40.

[34] *Id.* at 69.

[35] For example, the SEC should clarify that it would not be *per se* misleading for a fund with an 80% investment policy to invest in large-cap equities to invest up to 20% of its assets in small-cap equities or for a fund with an 80% investment policy to invest in equities generally to invest up to 20% of its assets in bonds or other fixed income instruments.

require funds and investment advisers to provide additional information regarding their ESG investment practices (the "ESG Proposal").[36] That proposal, if adopted, will, in effect, formalize three categories of investment strategies: "integration," "ESG focused" and "impact."[37] Separately, in 2020, the Commission proposed sweeping changes to the content and delivery requirements associated with prospectuses and shareholder reports.[38] The Commission's agenda indicates that it plans to finalize the shareholder reports proposal later this year.

The disclosure proposals represent significant changes in the scope and format of the information that would be provided to fund investors, and the ESG Proposal would introduce consequential new vocabulary for the classification of funds that consider ESG factors. We believe it would be premature for the Commission to finalize its approach to ESG in the Names Rule without allowing sufficient time, after implementation of these two disclosure proposals, to evaluate how investors' understanding and market practices are shaped by these new disclosure regimes. Moreover, it would seem difficult to conclude that certain names are *per se* misleading based on a fund classification vocabulary with which the Commission, investors and the market do not yet have any practical experience.

D. The Commission Should Clarify Guidance Related to Names with Multiple Elements

The Release provides guidance on the application of an 80% investment policy when a name suggests an investment focus that has multiple elements.[39] The examples in the Release present relatively straightforward scenarios such as a "Wind and Solar Power" fund or an "Environmental, Social, and Governance" fund.[40] This guidance, however, raises a number of questions that the examples do not answer.

We believe the Commission should, at a minimum:

- Provide additional clarity regarding the requirements for funds with multiple terms in their names, particularly ESG-related terms.

- Confirm explicitly that it will consider the overall context in which terms are used. For example, the Commission should recognize that certain terms are intended to be (and, indeed, are) read together in certain contexts or may not be solely used for ESG investment strategies. For example, "Sustainable Growth" could reasonably be read as an investment focus consisting either of two elements (*i.e.*, investing in companies that are sustainable in the environmental sense of the term) or of a single element (*i.e.*, growth that is sustainable over time). In addition, while the term "Impact" may be used in connection with ESG strategies, this is not exclusively the case.

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36 *See* Enhanced Disclosures by Certain Investment Advisers and Investment Companies about Environmental, Social, and Governance Investment Practices, Rel. Nos. IA-6034 & IC-34594 (May 25, 2022).

37 See *id*.

38 Tailored Shareholder Reports, Treatment of Annual Prospectus Updates for Existing Investors, and Improved Fee and Risk Disclosure for Mutual Funds and Exchange-Traded Funds; Fee Information in Investment Company, Release Nos. 33-10814, 34-89479, and IC-33963 (Aug. 5, 2020).

39 Release at 25-26.

40 *Id*.

IV. Comments on the Proposed Derivatives Requirements

A. The Commission Should Add Flexibility for Funds to Value Derivatives Using Exposure Metrics and Methods Other than Notional Value

The proposed amendments would require funds, in calculating assets for purposes of determining compliance with the Names Rule, to value derivatives instruments using their notional amounts, with certain adjustments.[41] The Commission acknowledges that the "value" of a derivatives instrument as defined in the Investment Company Act, which is generally the market value or fair value of securities, "may bear no relation to the investment exposure created by the derivatives instrument," and stated that this requirement is designed "to reflect the investment exposure derivatives investments create better and to increase comparability."[42] Although we generally support the proposed use of notional value for purposes of the Names Rule, for the reasons discussed below, we do not believe that requiring the use of notional value is necessary and that a more flexible approach would better capture the exposure funds obtain through all of their derivatives instruments.

We note that there can be varying methods used to calculate derivatives exposure based on a fund's purpose for holding a particular derivatives instrument (*i.e.*, gaining exposure to an underlying asset versus hedging or risk management purposes), and that the notional value of certain derivatives instruments may not adequately represent the exposure a fund obtains through such instruments and may lead to distortions in a fund's compliance testing and results. For example, a fund may have more than 80% of its net assets invested in investments suggested by the fund's name and should consequently be able to comply with its 80% test, but may also enter into derivatives transactions to protect against risks posed by investments not suggested by the fund's name (*i.e.*, investments not included in the 80% basket). Applying the notional value of such derivatives instruments, which would not be eligible for inclusion in the 80% basket, could have a potentially large impact on the denominator for purposes of the Names Rule compliance test and cause the fund to fail the test, even though the derivatives instruments are only used for hedging or other risk management purposes and their impact on the fund's performance might be insignificant.

Accordingly, instead of requiring funds to use notional value for purposes of Names Rule compliance testing, we recommend that the Commission modify the proposed amendments to permit funds to test each derivatives instrument type consistent with a reasonable exposure metric and method that best measures the economic exposure the derivatives instrument obtains synthetically (which may or may not represent the notional value of the derivatives instrument), as long as funds consistently apply the relevant metric and method. Providing funds with the necessary flexibility to determine the measurement that most accurately captures their derivatives exposures, rather than mandating notional value testing for all derivatives, would be a reasonable approach, more efficient and practical from an operational standpoint, and would more closely align fund names with the economic exposure obtained through the fund's investments.

We believe this approach would be consistent with the Commission's recognition that valuation of derivatives through metrics other than notional value may be appropriate in certain other compliance contexts,[43] and the Commission's apparent understanding that a mandatory approach with respect to

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41 *Id*. at 48.

42 *Id*. at 49.

43 For example, in 2011, the Commission sought information on whether funds consider "current market value or the notional amount of a derivative (or some other measure)" in testing for compliance with concentration

utilization of notional value testing across all derivatives instrument types may not align a fund's compliance testing with the true economic exposure of a fund's derivatives transactions. Such alignment is particularly important in the context of the Names Rule and preventing the use of misleading or deceptive fund names.

B. The Commission Should Add Flexibility for Funds to Use or Not Use Adjustments for the Notional Value Calculation

The proposed amendments would require a fund, in calculating notional amounts for Names Rule purposes, to convert interest rate derivatives to their 10-year bond equivalents and to delta adjust the notional amounts of options contracts (the "Proposed Notional Adjustments").[44] In the Release, the Commission indicated that "requiring these tailoring adjustments is appropriate for purposes of the [N]ames [R]ule in order for a fund's 80% investment policy to best reflect the fund's investment exposure, which in turn would help ensure that the investment focus a fund's name communicates is not materially deceptive or misleading."[45]

Funds should be permitted, but not required, to make the Proposed Notional Adjustments in calculating notional amounts, which would be consistent with the adjustments permitted under Rule 18f-4 under the Investment Company Act for calculating a fund's "derivatives exposure."[46] It is our understanding that the Commission will receive comments from industry participants supporting greater flexibility with respect to the use of the Proposed Notional Adjustments, which have been implemented by some funds groups for purposes of Rule 18f-4, but not by other fund groups that have found it unnecessary to do so based on their limited derivatives user funds' levels of derivatives exposure and in light of the costs and operational challenges associated with implementing such adjustments in practice. We urge the Commission to take into consideration this information, which will indicate that the mandatory approach under the Proposed Notional Adjustments is overly limiting and may impose significant costs and operational challenges associated with implementing such adjustments in practice.

Many funds rely on third-party systems to monitor compliance with investment guidelines, policies, and applicable regulatory requirements, and such systems would need to undergo complex and expensive updates to incorporate the Proposed Notional Adjustments. The proposed mandatory approach could be cost-prohibitive and poses significant technological and operational burdens for funds that have not otherwise implemented the Proposed Notional Adjustments in connection with Rule 18f-4, which could be particularly disadvantageous for smaller fund groups and will lead to additional costs that are ultimately borne by fund shareholders.

We also note that a fund still would be subject to the codification in the Names Rule of the Commission's position that compliance with the Names Rule is not a safe harbor from Section 35(d)'s prohibition on funds' use of materially deceptive or misleading names (as discussed in more detail herein), which would serve to ensure that the Commission's goal underlying the required Proposed Notional Adjustments is met.

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requirements. Use of Derivatives by Investment Companies under the Investment Company Act, SEC Release No. IC-29776 (Aug. 31, 2011), available at www.sec.gov/rules/concept/2011/ic-29776.pdf.

[44] Release at 51-52.

[45] Id. at 52.

[46] 17 C.F.R. § 270.18f-4.

C. The Commission Should Clarify that the Provision Allowing Inclusion of Derivatives Providing Investment Exposure to Market Risk Factors Associated with the Investments Suggested by a Fund Name Is Not Intended to Have a Narrow Application

The proposed amendments would permit a fund to include in its 80% basket a derivatives instrument that provides investment exposure to one or more of the market risk factors associated with the investments suggested by the fund's name.[47] In the Release, the Commission highlighted interest rate risk, credit spread risk, and foreign currency risk as examples of such market risk factors, and enumerated the specific cases of currency forwards or swaps used to hedge foreign currency risk and interest rate swaps used to hedge interest rate risk and/or manage duration.[48]

While we generally support the proposed ability for a fund to include additional types of derivatives instruments in its 80% basket, we believe additional clarity from the Commission that the provision is not intended to be applied in a narrow manner is needed. The Commission has acknowledged in the context of Rule 18f-4 that there are many potential market risk factors related to fund investments[49] and the Commission should acknowledge in adopting the Names Rule that it would permit funds to take into account all derivatives that provide exposure to such risk factors for purposes of Names Rule compliance testing.

Furthermore, funds that use derivatives instruments that complement the fund's strategy, but that do not provide investment exposure to the enumerated market risk factors in the Release, might be disadvantaged and unable to comply with their 80% policies. In the absence of the requested guidance, we believe the ambiguities associated with the proposed approach increase the risk that Commission examination staff will make negative comments regarding the determinations of a fund to include in its 80% basket derivatives instruments that are not of the types enumerated in the Names Rule or the Release. Such negative comments could lead to adverse consequences, such as required disclosures in a fund's offering documents. We do not believe the Commission intends for the proposed amendments to result in such an outcome and do not believe that it would be appropriate for Commission examination staff to issue such negative comments.

D. The Commission Should Permit Funds to Exclude Closed-Out Positions with Different Counterparties

The Commission's Request for Comment #33 suggests that a fund would eliminate from the calculation of its compliance with the Names Rule "derivatives that were closed out with the same counterparty and result in no credit or market exposure to the fund."[50] The Commission asked whether the Names Rule should address these positions and which positions funds currently treat as closed-out when determining

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[47] Release at 55.

[48] *Id.*

[49] *See* the definition of "Value-at-Risk" or "VaR" under Rule 18f-4(a) which states that a fund's compliance with the relative VaR test or the absolute VaR test must "take into account and incorporate all significant, identifiable market risk factors associated with a fund's investments, including, as applicable (i) equity price risk, interest rate risk, credit spread risk, foreign currency risk and commodity price risk; (ii) material risks arising from the nonlinear price characteristics of a fund's investments, including options and positions with embedded optionality; and (iii) the sensitivity of the market value of the fund's investments to changes in volatility." 17 C.F.R. § 270.18f-4.

[50] Release at 60.

compliance with the Names Rule.[51] We do not believe that funds should be limited to excluding closed-out positions with the same counterparty for purposes of Names Rule compliance testing and recommend that the Names Rule explicitly permit exclusion of all closed-out derivatives positions, regardless of whether they are closed out with the same counterparty or are the same instrument type.

We acknowledge that the proposed approach is consistent with the types of closed-out derivatives funds can disregard for calculating derivatives exposure under Rule 18f-4. However, we do not believe there is a compelling policy reason to restrict closed-out positions to derivatives closed out with the same counterparty for Names Rule compliance purposes and note that the policy concerns underlying Section 18 and Rule 18f-4 are not applicable to the Names Rule. Section 18 and Rule 18f-4 aim to address the risks associated with funds holding a large volume of open derivatives positions with various counterparties that are all subject to separate margin and other requirements and the risk of a fund counterparty defaulting while the other position remains outstanding. Section 35 and Rule 35d-1, on the other hand, focus primarily on addressing the alignment between the investment exposures suggested by a fund's name and those resulting from the fund's investments and preventing the use of misleading fund names. The identity of the counterparties is not relevant to and should not impact a fund's elimination of its investment exposure through closed-out derivatives positions. If the counterparty to the second transaction defaults, the fund simply would start counting the exposure under the remaining derivatives instrument for purposes of the Names Rule. We believe this less restrictive approach is reasonable and would result in closer alignment between Names Rule compliance testing and common industry practices with respect to offsetting derivatives transactions.

Furthermore, we believe that limiting excluded closed-out derivatives positions to those with the same counterparty would lead to economic inefficiencies and could be detrimental to a fund's returns. Under the proposed approach, a fund might be compelled to transact with the counterparty with which it entered in the original derivatives transaction on less favorable terms, including pricing, or which poses more credit risk to the fund, than a different counterparty with which it could enter into an offsetting position at the time it needs to eliminate its exposure under the first transaction.

If the Commission does not permit funds to exclude all offsetting derivatives positions for Names Rule purposes, we urge the Commission to at least provide guidance that funds may treat all centrally cleared derivatives transactions as positions with the same counterparty for purposes of determining closed-out positions.

E. The Commission Should Permit Funds to Include Physical Short Sales and Short Positions in Their 80% Baskets and Address Valuation of Physical Short Sales

The Commission's Request for Comment #39 states that a fund would be required to take into account the notional value of short positions in derivatives for purposes of determining compliance with its 80% test and asks whether this treatment is appropriate.[52] The Commission also sought comment on whether the Names Rule should address the consideration and valuation of physical short sales for purposes of Names Rule compliance.[53]

We believe that the Commission should adopt a flexible approach to permit, but not mandate, funds to include physical short sales and short derivatives positions that provide short investment exposure to the

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[51] *Id.*

[52] *Id.* at 63-64.

[53] *Id.*

investments suggested by the fund's name or to the market risk factors discussed herein in their 80% baskets. Funds should be allowed to include in their 80% baskets the absolute value (however measured) of such a short sale or short position, regardless of whether the fund's name specifically suggests the use of short sales or short positions. It is our understanding that many fund groups consider relevant short exposures in their 80% baskets for purposes of Names Rule compliance testing, even in instances where a fund's name might not suggest the fund has such exposure in its portfolio. So long as a fund discloses that it may utilize short positions as part of its investment strategy, a fund's name would not need to include specific terminology indicating as much.

The Release and the proposed amendments do not provide specific guidance with respect to how physical short sales should be valued for Names Rule purposes and we urge the Commission to provide such guidance and clarity. Physical short sales are commonly used by various types of funds and the Commission should adopt a flexible approach under which funds could utilize the absolute notional amount or the absolute market value of the asset sold short under a physical short sale for purposes of valuing such transaction for Names Rule compliance. In addition, a fund should be permitted to look through to the components of its open short sale positions to offset their investment exposure (i.e., the fund should be able to close-out all or part of a short sale position) for purposes of compliance with its 80% policy. We believe that the current lack of clarity regarding physical short sales may cause confusion and divergent practices among the industry.

F. The Commission Should Expand the Deduction for Cash and Cash Equivalents

The proposed amendments would require funds to deduct cash and cash equivalents up to the notional amounts of the fund's derivatives instruments from a fund's assets when computing compliance with the Names Rule (i.e., the denominator in the 80% calculation).[54] The proposed approach is designed to remove from the calculation cash and cash equivalents, which do not themselves provide market exposure, where they effectively function as low risk collateral for the derivatives instruments whose notional amounts already are included in the denominator and to eliminate "double counting" the fund's exposure.[55] While we are generally supportive of this approach, for the reasons detailed below, we strongly urge the Commission to expand the types of assets that funds may exclude beyond cash and "cash equivalents."

The proposed exclusion is needlessly restrictive and ignores the reality that funds use many different types of liquid investments for cash management purposes similar to the manner in which the Commission describes the employment of cash and cash equivalents in connection with derivatives instruments. Funds that are heavy derivatives users and that have derivatives-focused strategies frequently hold assets other than cash and cash equivalents that also effectively function as low-risk collateral for derivatives instruments. It is our understanding that such assets may reduce a fund's exposure to bank borrowings and likely have a limited impact on fund returns, but are not typically acquired to help the fund obtain specific market exposure.

We believe the Commission should provide guidance allowing funds to exclude any assets that are posted as collateral under derivatives instruments and certain other asset types, including other U.S. government securities such as U.S. Treasury securities with under five years to maturity and comparable non-U.S. government securities permitted to be posted as margin under Commodities Future Trading Commission's and prudential regulators' margin requirements, investment-grade corporate bonds with under three years to maturity, short-term bond fund shares, interests in other short-term investment funds, and repurchase

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54 *Id.* 53-54.

55 *Id.*

agreements on cash equivalents or any of the foregoing types of instruments. Funds should also be permitted to exclude other categories of securities or assets that also effectively function as low-risk collateral for derivatives instruments held in a fund's portfolio that provide exposure to the fund's investment focus.

G. The Commission Should Clarify that Derivatives Valuation Methods Under the Names Rule May Differ than Those for Other Investment Company Act Requirements

We strongly urge the Commission in adopting the Names Rule to clearly state that derivatives instruments may be valued differently under the Names Rule than for purposes of assessing compliance with other Investment Company Act requirements, including with respect to diversification and portfolio concentration policies. The guidance from the Commission should underscore that any valuation methods permitted for derivatives valuation under other rules or under U.S. GAAP are not subject to change as a result of the proposed amendments and that any adopted prescribed valuation method is required to be used only for Names Rule compliance purposes. Such an acknowledgement would provide much needed clarity to funds and investors in an increasingly complex regulatory environment and help ensure fund compliance with all applicable requirements under the Investment Company Act.

V. Unlisted Closed-End Funds and BDCs; Insurance Company Separate Accounts Classified as Unit Investment Trusts

A. The Proposed Requirement that Unlisted Closed-End Funds and BDCs Adopt Fundamental 80% Investment Policies Is Overly Restrictive

The Commission proposes to require any unlisted closed-end fund or BDC that must adopt an 80% investment policy to make such policy fundamental.[56] As a result, unlike open-end funds and traded closed-end funds, an unlisted closed-end fund or BDC would need to seek shareholder approval for any change that deviates from its 80% investment policy. The Release states that such a requirement would be appropriate because shares of unlisted closed-end funds and BDCs are relatively illiquid, and, therefore, their shareholders are not able to redeem or sell their shares within the notice period preceding a change in the fund's 80% investment policy in the event that they disagree with the change.[57]

We believe that the Commission's proposed rule is overly broad and should not be adopted. As proposed, the requirement will significantly impede a fund's ability to make strategy changes that the fund and its board deem to be in the best interest of the fund and its shareholders.

If the Commission determines to adopt a form of this requirement, we believe it should be limited so as to provide a mechanism for unlisted closed-end funds and BDCs to continue to maintain non-fundamental 80% investment policies. For example, the Commission could provide an exemption for funds that provide a repurchase or tender opportunity to all shareholders as of the date the fund provides notice of the planned change, in accordance with applicable Commission rules, within a notice period. Alternatively, for funds that offer regular repurchases or tender offers, such funds should be permitted to set a notice period for a proposed 80% investment policy change that is lengthy enough for any investors who held shares as of the date the fund provides notice of the planned change and wish to redeem their investments to do so prior to

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56 Release at 65-66.

57 *Id.* at 66-67.

the change in policy. An unlisted closed-end fund or BDC should be permitted to change its 80% investment policy once adequate notice is provided and a subsequent repurchase or tender offer is undersubscribed.

B. The Commission Should Remove the Fundamental Policy Requirement for Non-Traded BDCs to Restore the Greater Investment Policy Flexibility Congress Intended BDCs to Have

In 1980, Congress created BDCs as a specialized type of closed-end fund whose principal activities consist of investing in, and offering to provide "significant managerial assistance" to, small, growing or financially troubled operating companies.[58] These companies generally are unable to obtain financing from traditional sources (*e.g.*, banks or capital markets). To this end, a BDC is required to invest at least 70% of its portfolio assets in cash (or high quality, short-term debt securities), securities issued by financially troubled businesses or securities issued by "eligible portfolio companies" (*i.e.*, among other things, companies organized and with their principal place of business in the United States).[59]

The characteristics and geographic location of the issuers in which BDCs must invest distinguish them from other closed-end funds. Congress also provided BDCs with greater operating flexibility than other closed-end funds or mutual funds. In particular, to "change the nature of its business so as to cease to be, or to withdraw its election as, a [BDC]," a BDC must first seek shareholder approval.[60] The House Report accompanying the 1980 legislation that created BDCs explains that this requirement is in lieu of "the more sizable number of instances for which shareholder approval is required under present Section 13 of the [Investment Company Act]."[61]

The proposed rule amendments' fundamental policy requirements do not distinguish between BDCs and other investment companies. Consequently, BDCs would be subject to the same shareholder vote requirements as registered investment companies. This result would undermine the clear Congressional intent that BDCs be permitted greater operating flexibility in this respect than registered investment companies. Accordingly, we recommend that the Commission revise the proposed fundamental policy restrictions to distinguish BDCs from registered investment companies, consistent with clear Congressional intent.

C. Insurance Company Separate Accounts Classified as Unit Investment Trusts

We believe that the Commission should, through guidance or otherwise, expressly exclude from the 80% investment policy requirement and any related recordkeeping requirements of the proposed amendments to the Names Rule sub-accounts of insurance company separate accounts classified as unit investment trusts ("UITs") that fund variable annuity contracts and variable life insurance contracts when the sub-account invests in a single, designated underlying fund in reliance on Section 12(d)(1)(E) of the Investment Company Act and has substantially the same name as the corresponding underlying fund. We believe this exclusion to be appropriate because, in this specific context, no legitimate investor protection concerns are

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58 *See* 15 U.S.C. §§ 80a-2 and 80a-54.

59 *Id.*

60 15 U.S.C. §§ 80a-57.

61 S.R. Report No. 96-958 at 33 (1980); H.R. Report No. 96-1341 at 51-52 (1980).

raised by these two-tier sub-accounts of UIT separate accounts because, among other things, the names of these sub-accounts are, to our knowledge, not used in marketing materials. Further, we believe that the 80% investment policy requirement and any related recordkeeping requirements of the proposed amendments to the Names Rule would—if applied to these sub-accounts of UIT separate accounts—be unnecessary and duplicative of applicable law and regulation, notably in light of Section 12(d)(1)(E) with respect to the sub-account of the UIT separate account and the Names Rule with respect to the underlying fund, and could result in significant recordkeeping and other burdens for insurance companies that do not serve any meaningful policy purpose.

VI. The Benefits of the New N-PORT Reporting Would Not Support the Costs

A. The Proposed Amendments

The proposal would impose several new reporting requirements on Form N-PORT, the form the Commission uses for collecting detailed monthly data about most registered funds.[62] Specifically, a fund would need to report: (1) whether an individual portfolio investment is included in a fund's 80% basket, (2) the total value of a fund's 80% basket (as a percentage of the fund's total assets), and (3) the number of days during the reporting period that the fund was not in compliance with its 80% investment policy.[63]

1. The Proposed Form N-PORT Reporting Requirements Impose Significant and Unjustified Costs

We believe the proposed requirement to report whether each investment in a fund's portfolio is included in the fund's 80% basket would impose significant direct and indirect costs. For example, funds are likely to incur significant compliance costs, including a need to engage third-party data providers capable of coding a fund's investments and mapping them to its 80% investment policy, which may be passed along to shareholders. This substantial direct burden is also likely to result in an indirect cost to investors because it would disincentivize the use of names that are descriptive.

At the same time, it is not clear what benefit is gained in requiring classification of 100% of a fund's portfolio investments when only 80% are required to satisfy its 80% investment policy. In addition, we do not believe that the requirement that funds subject to an 80% investment policy classify each portfolio investment serves any meaningful public policy objective, particularly in light of the related proposal to require funds to report the total value of the investments within their 80% basket as a percentage of the fund's assets. Accordingly, we believe the Commission's economic analysis is drastically understated, particularly as it relates to implementation, and we oppose this reporting.

We also believe that funds should not be required to publicly report the number of days in which a fund was not in compliance with its 80% investment policy. In this regard, the Commission should align its approach with that of relevant aspects of analogous reporting requirements under other Commission rules, which are not made publicly available.[64] While this information may be of use to the Commission in

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62 Release at 95-96, 100.

63 *Id.*

64 *See, e.g.*, Use of Derivatives by Registered Investment Companies and Business Development Companies, Release No. IC-34084 (October 28, 2020); Investment Company Liquidity Disclosure, Release No. IC-33142 (June 28, 2018).

monitoring the industry's compliance with the Names Rule, we believe that presenting this to investors publicly on Form N-PORT, devoid of context and explanation as to the cause or effect of the deviation, would not communicate meaningful information to investors and risks creating unnecessary confusion.

2. Alternative Approaches

For the reasons explained above, we do not support the requirement to classify on Form N-PORT 100% of a fund's holdings. As an alternative, the Commission should instead adopt an approach that more appropriately balances the usefulness of the information to shareholders with the costs associated with the proposal. In this regard, it would be reasonable to require a fund to indicate in an appropriate filing whether the fund is subject to an 80% investment policy. Such an approach would give investors clear notice that a fund is subject to an 80% investment policy when reviewing the fund's portfolio holdings.

VII. The Proposed Recordkeeping Requirements Are Burdensome and Unnecessary

A. The Proposed Amendments

The proposed amendments would impose numerous new recordkeeping requirements.[65] These would include written records relating to: (1) which portfolio investments are included in a fund's 80% basket and the basis for including each investment in the basket; (2) the value of a fund's 80% basket as a percentage of the fund's assets; (3) the dates of any deviations from a fund's 80% investment policy together with documented reasons for such deviations; and (4) any notices sent to shareholders under the Names Rule.[66]

In addition, the proposed amendments would also require funds that do *not* adopt an 80% investment policy to maintain a written record documenting the basis for concluding that the fund's name does not require adoption of such a policy.[67]

1. The Proposed Recordkeeping Requirements Are Unduly Burdensome

The proposed requirement that a fund maintain records documenting each investment included in the fund's 80% bucket and the basis for its inclusion would impose significant direct and indirect costs. For example, a fund's compliance and portfolio management personnel would need to devote significant time to documenting the basis for including each investment, even in cases where an investment is held for a short period of time.[68] This will distract such personnel from other critical aspects of fund compliance and portfolio management. Not only would this requirement significantly increase compliance costs for each fund, but together with the Commission's proposed expansions in the scope of the Names Rule, more funds would be subject to this recordkeeping requirement. In addition, the expansion of the rule to encompass terms used in names that will not be susceptible to objective, quantifiable tests would mean that the task

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65 Release at 103-104, 106-107.

66 *Id.* at 103-104.

67 *Id.* at 106-107.

68 For example, some funds engage in frequent trading and may even hold certain investments for a single day or less than a day. Documenting whether or not such investments were part of the fund's 80% basket would be particularly burdensome, without any measurable benefit.

of documenting the basis for each determination would be even greater than if the recordkeeping requirement were imposed without expanding the scope of the rule.

At the same time, the Commission has identified little benefit to funds and their shareholders of creating and maintaining such detailed records. While the Release seeks to justify this requirement by reference to the Commission's ability to better evaluate whether a fund is complying with its 80% investment policy, the Commission presents no data to show that compliance with these policies is currently a concern.

2. Alternative Approaches

We believe that the new recordkeeping requirements are unnecessary and that, at a minimum, the Commission should not adopt the requirement that a fund maintain records documenting each investment included in its 80% bucket and the basis for its inclusion.

If the Commission determines to adopt these requirements, we respectfully recommend that it provide clearer guidance as to the types of records that would be required, particularly with respect to records substantiating the inclusion of a particular investment in a fund's 80% bucket. Additionally, the Commission should provide guidance on how such a recordkeeping requirement would apply to index funds and the underlying index constituents.

We also believe the Commission should not adopt the requirement that funds without an 80% policy must document the basis for concluding that the fund's name does not require one. This proposed amendment would unnecessarily extend the Names Rule to every fund, regardless of its name. The implication of such an amendment is that funds bear the burden of demonstrating when the Names Rule does not apply. Requiring a fund to affirmatively show that a rule does not apply is inconsistent with the general approach of the federal securities laws and not supported by the arguments presented in the Release.

VIII. The Proposed Compliance Date Provides Insufficient Time

In light of the significant changes that the Commission has proposed, a compliance period of one year from adoption is insufficient.[69] Implementing these changes would demand significant time from legal, compliance and operations personnel, particularly because of the breadth of, and numerous interpretive challenges that would result from, the proposed amendments. For example, the proposed amendments would require fund sponsors to (1) evaluate the impact of amendments to the Names Rule on existing funds; (2) determine what, if any, changes need to be made to the funds' investment strategies and names; (3) seek approval of such changes, as appropriate, from the funds' boards of directors/trustees and/or shareholders; (4) adopt policies and procedures and design, modify or acquire systems to comply with the funds' new investment strategies and the broader amendments to the Names Rule, including the new N-PORT and recordkeeping requirements; and (5) amend the funds' prospectuses and/or statements of additional information to disclose any amended investment policies or strategies.

Many fund sponsors would likely need to engage third-party service providers to assist in conducting ongoing assessment of fund portfolios. These service providers will, in turn, require considerable time to develop and test the systems and capabilities necessary to support these activities.

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[69] *See* Release at 111-112.

If the Commission adopts the proposed amendments, all registered funds are likely to face compliance burdens, ranging from evaluating the impact of the amendments to making significant legal and operational changes. As a result, we believe the Commission's estimates of the time, resource and costs of the proposed amendments are dramatically understated. When the Commission evaluates at adoption the costs of the amendments and the time permitted to come into compliance, it must consider not only the scope of these burdens but also that many funds will face these burdens concurrently because of common fiscal year ends. This will undoubtedly strain the limited number of third-party service providers in addition to adviser personnel.

Moreover, the Commission should not evaluate the compliance date of the Names Rule in isolation. The Commission has proposed numerous, sweeping changes affecting registered funds, and the Commission's regulatory agenda presages more to come. While the Commission has not provided a precise roadmap of proposals, adoptions and compliance dates, it appears likely that funds will face multiple, overlapping compliance periods of significant rulemakings for years to come. The resources required to meet each of these compliance dates are likely to overlap significantly, meaning that the burden of compliance and the time required must be evaluated cumulatively, and the Commission should recognize that the marginal cost of implementation increases with each additional change that it mandates.

Accordingly, the Commission should provide funds with at least three years to come into compliance with any amendments to the Names Rule. Where the Commission has not identified the need for rapid implementation, a shorter compliance period appears unjustified.

IX. Cost/Benefit Analysis

The cost/benefit analysis set forth in the Release is flawed and does not adequately reflect the true burden that implementation of and compliance with the amended Names Rule would impose on funds and their sponsors, many of which are discussed above.[70]

Further, we believe the Commission has significantly underestimated the number of annual update filings that would be required to be made pursuant to Rule 485(a) under the Securities Act of 1933, as amended, which would impose considerable additional costs on fund sponsors and place significant burdens on the Commission's disclosure review staff.

Additionally, many funds explicitly reference the existing Names Rule's "under normal circumstances" standard in their 80% investment policies. Under the proposal, the use of this standard would no longer be permissible and, presumably, all of these funds would need to amend their policies to comply with the new standard. Thus, the Commission's cost/benefit analysis appears to have drastically underestimated the number of funds that would be required to change their names as a result of the proposed amendments, which would include the significant expenses associated with obtaining shareholder approval in some cases. To the extent that the Commission determines to alter the current "under normal circumstances" standard, it should provide interpretive guidance as to whether each such fund would be required to provide notice of such a change or, in the case of a fund with a fundamental 80% investment policy, to obtain shareholder approval of the change.

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[70] *See, supra*, Sections II(A), VI and VII.

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We appreciate the opportunity to provide comments on the proposed amendments to the Names Rule. Please feel free to contact Philip T. Hinkle at [redacted], Corey F. Rose at [redacted], Matthew E. Barsamian at [redacted] or Nadeea R. Zakaria at [redacted] with any questions about this submission.

Very truly yours,

/s/ Dechert LLP

Dechert LLP