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Submitted by SEC Webform (http://www.sec.gov/rules/submitcomments.htm)

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

RE: File No. S7-16-22: Investment Company Names; File No. S7-17-22: Enhanced Disclosures by Certain Investment Advisers and Investment Companies about Environmental, Social, and Governance Investment Practices

Dear Ms. Countryman:

On behalf of the North American Securities Administrators Association, Inc. ("NASAA"),[1] I am writing in response to U.S. Securities and Exchange Commission ("SEC" or the "Commission") Release No. IC-34593, *Investment Company Names* (the "IC Names Proposal") and Release No. IA-6034, *Enhanced Disclosures by Certain Investment Advisers and Investment Companies about Environmental, Social, and Governance Investment Practices* (the "Disclosure Proposal") (collectively, the "Proposals").[2]

Taken together, the Proposals seek to ensure that investors have access to clear, complete, and accurate information so that they can make informed decisions about how to invest their money. NASAA supports this goal. When an investment adviser (an "Adviser") or a registered fund (a "Fund") chooses to adhere to a particular strategy or philosophy and holds itself out accordingly, it is crucial that the Adviser or Fund explains itself to investors truthfully, accurately, and fulsomely. As we expressed in our Legislative Agenda for the 117th Congress, NASAA is particularly concerned about the phenomenon of "greenwashing"[3] and we support efforts to

[1] Organized in 1919, NASAA is the oldest international organization devoted to investor protection. NASAA's membership consists of the securities administrators in the 50 states, the District of Columbia, Canada, Mexico, Puerto Rico, and the U.S. Virgin Islands. NASAA is the voice of securities agencies responsible for grass-roots investor protection and efficient capital formation.

[2] The IC Names Proposal is available at https://www.sec.gov/rules/proposed/2022/ic-34593.pdf and the Disclosure Proposal is available at https://www.sec.gov/rules/proposed/2022/ia-6034.pdf.

[3] NASAA Legislative Agenda for the 117th Congress at 8-9, *available at* https://www.nasaa.org/wp-content/uploads/2022/07/NASAA-Legislative-Agenda-for-the-117th-Congress-updated-7-7-22.pdf.

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protect investors from selective and misleading disclosures about the environmental, social, or other purported benefits of investment products and services.

I. The IC Names Proposal Would Benefit Investors by Bringing More Discipline and Clarity to Fund Naming Practices.

Funds play a key role in retail investors' ability to save for retirement, college, and other significant financial needs. Investors today have access to a multitude of different Funds, representing a variety of philosophies, focuses, and strategies.[4] The variety of available Funds makes choosing a Fund an exceptionally complex task for most investors. As a result, many investors rely on Fund names for information about a Fund's essential characteristics, including its investment style, strategies, and risks.[5] Indeed, a Fund's name is typically the first piece of information that investors receive about the Fund, and that first impression can exert a powerful influence over investors' investment decisions.[6] NASAA generally supports the IC Names Proposal and we offer the following comments for the Commission's consideration.

The Commission adopted Rule 35d-1[7] (the "Names Rule") in 2001 "to address certain [Fund] names that are likely to mislead an investor about a [Fund's] investment emphasis."[8] The Names Rule rests on the fundamental premise that when a Fund elects to adopt a name that it will focus its investments in a particular way, the Fund must actually invest in such a manner that "the name will accurately reflect the company's investment policy."[9] Among other things, the Names Rule requires that if a Fund's name indicates a focus on a particular "type of investment" (such as stocks, bonds, or money market instruments[10]), investments in particular industries, or investments

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4 *See* IC Names Proposal at 117-18 (data indicating that, as of July 2021, there were more than 13,000 Funds that accounted for more than $31 trillion in total net assets).

5 *See*, *e.g.*, Anne-Florence Allard, Jonathan Krakow, and Kristien Smedts, *When mutual fund names misinform*, at 2 (June 16, 2020), *available at* https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3628293 (noting that "investors rely on information or heuristics summarising key mutual fund characteristics [such as] past performance, explicit fees, or base their decision on qualitative information such as a fund name or its ticker symbol," and noting previous research on the subject). *See also Final Rule: Investment Company Names*, SEC Release No. IC-24828, 66 FR 8509, 8510 (Jan. 17, 2001) ("Names Rule Adopting Release") (noting that Fund names "may communicate a great deal to an investor").

6 *See*, *e.g.*, Allard et al. at 2; Ben Carlson, *What's In a (Mutual Fund's) Name?*, A WEALTH OF COMMON SENSE (Mar. 10, 2015), https://awealthofcommonsense.com/2015/03/whats-in-a-mutual-funds-name/ ("Unfortunately, Wall Street's team of marketers and salespeople know that investors look at the names of the funds when making their investment choices. And when they don't like how the fund's name is currently working, they can always change it."); Silla Brush, *One Fund, Three Names and Lots of Questions for 'ESG': From "impact" to "ESG" to "sustainable," a BlackRock fund rebrands and rebrands again—and millions flow in*, BLOOMBERG (updated July 25, 2022, 9:26 AM EDT), https://www.bloomberg.com/news/articles/2022-07-25/how-blackrock-rebranded-one-sustainable-mutual-fund.

7 17 CFR 270.35d-1.

8 Names Rule Adopting Release, 66 FR at 8509.

9 *Id.* at 8511.

10 *Id.* at 8510.

within particular geographical areas, the Fund must have a policy to invest at least 80% of the value of its assets accordingly "under normal circumstances." In the twenty-one years since the Names Rule was adopted, the Fund industry and the securities markets more broadly have changed dramatically, as explained in the proposal.[11]

a. Fund Names Suggesting an Investment Focus

The IC Names Proposal would expand the Names Rule so that the 80% requirement would apply not only to the categories of investment currently specified in the Names Rule, but also to any Fund name that suggests that the Fund focuses on investments that have, or whose issuers have, certain characteristics. This would include names with terms such as "growth" or "value," as well as names that indicate that a Fund incorporates ESG factors. Because the IC Names Proposal would expand the logic of the Names Rule to a wider scope of Funds whose names serve as the initial bases upon which investors make investment choices, the IC Names Proposal enhances investor protections and the Commission should expand the 80% requirement as proposed.

We agree that Fund names included in the proposed expanded scope communicate to investors, and create reasonable expectations that the Funds will focus on investments and issuers that have the specified characteristics. Furthermore, the proposed approach – to make no distinction between types of investments and investment strategies – is the correct one. In the investment context, terms such as "growth" and "value" have established meanings and are likely to create reasonable expectations among investors that such Funds will focus on companies that have certain characteristics. For example, investors would reasonably expect a "growth" Fund to focus on companies that are expected to grow faster than their industry peers or the broader economy, while investors would reasonably expect a "value" Fund to focus on companies that appear undervalued by the market based on their fundamentals. Similarly, although terms such as "ESG," "sustainable," "green," and "socially responsible" can mean different things to different people, these terms are not devoid of accumulated meaning. Funds choose these terms specifically for their marketing power.[12] Further, the IC Names Proposal grants Funds a certain degree of latitude to define these terms for themselves in their prospectuses. Specifically, the IC Names Proposal explains that "Funds have flexibility to use reasonable definitions of the terms that their

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[11] *See* IC Names Proposal at 12-13, 117-19.

[12] *See* Alicia Adamczyk, *Why 'greenwashing' is an issue for sustainable investments – and how to avoid it*, CNBC.com (Apr. 23, 2021), https://www.cnbc.com/2021/04/23/what-to-know-about-greenwashing-in-sustainable-investments html (noting that "[n]ew investments in sustainable funds more than doubled in 2020 compared to 2019, reaching a record-high $51 billion"); MBC Strategic, *Why ESG Investment Marketing is More Important Than Ever* (Dec. 15, 2020), https://mbcstrategic.com/why-esg-investment-marketing-is-more-important-than-ever/; Ben Carlson, *What's In a (Mutual Fund's) Name?*, A WEALTH OF COMMON SENSE (Mar. 10, 2015), https://awealthofcommonsense.com/2015/03/whats-in-a-mutual-funds-name/ ("Unfortunately, Wall Street's team of marketers and salespeople know that investors look at the names of the funds when making their investment choices. And when they don't like how the fund's name is currently working, they can always change it.").

names use," as long as those definitions are not inconsistent with the terms' plain English meaning or established industry use.[13]

We also believe that this change would apply to Fund names suggesting a focus on other trendy "'thematic' areas" noted in the IC Names Proposal, including cybersecurity, blockchain/digital assets, and artificial intelligence.[14] However, the IC Names Proposal does not address these areas in the context of the proposed expanded scope. Ideally, the IC Names Proposal should extend the Names Rule to apply – as a matter of principle – to any Fund name that suggests a particular investment focus or strategy. That appears to be the intention of the proposal, but the proposed rule text could be read to limit the scope of the proposed expansion. Investors, Funds, and regulators would nevertheless be well served by greater clarity on whether the proposed expansion would reach these and other areas of potential investment focus.[15]

b. Temporary Departure from the 80% Requirement

The IC Names Proposal would also specify the circumstances under which a Fund may temporarily depart from the 80% requirement and would impose a 30-day time limit on temporary departures in certain circumstances. This would replace the current requirement that the 80% requirement apply at the time of investment and "under normal circumstances." Under the current rule, it is generally up to a Fund to determine when circumstances are other than "normal," and there is no set time limit on such departures. The status quo therefore increases the risk that a Fund's investments will not be consistent with its name over an extended period and investors will be misled.

We believe that the proposed amendment would protect investors by bringing more certainty in the Names Rule and ensuring that Funds remain vigilant about their obligations under the Names Rule. We also believe that the proposed circumstances permitting temporary departure are reasonably tailored to permit departure from the 80% requirement only where doing so is not reasonably avoidable or is necessary to protect against investor losses. However, we would support a more flexible approach that permits a longer period of departure in the case of extreme market disruptions,[16] or where a Fund needs to take a defensive position in cash or cash equivalents in order to avoid severe investor losses or exit restrictions.

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13 IC Names Proposal at 74-75.

14 *See id.* at 13.

15 *See id.* at 12-13; *see also* Will Ashworth, *18 Bitcoin ETFs and Cryptocurrency Funds You Should Know*, KIPLINGER (Apr. 12, 2022), https://www.kiplinger.com/investing/cryptocurrency/603600/bitcoin-etfs-cryptocurrency-funds (describing "18 ways to ride the crypto wave"); Evelyn Cheng, *$24 million iced tea company says it's pivoting to the blockchain, and its stock jumps 200%*, CNBC.COM (updated Dec. 26, 2017), https://www.cnbc.com/2017/12/21/long-island-iced-tea-micro-cap-adds-blockchain-to-name-and-stock-soars.html.

16 *See*, *e.g.*, Comm'r Hester M. Peirce, *Statement on Investment Company Names* (May 25, 2022), https://www.sec.gov/news/statement/peirce-fund-names-statement-052522#_ftnref2 (asking whether "a fund with an emphasis on emerging markets in central Europe [would] have been able to get right with this rule 30 days following Russia's invasion of Ukraine").

c. Unlisted Closed-End Funds and Business Development Companies ("BDCs")

The IC Names Proposal would additionally establish that an 80% investment policy established by an unlisted closed-end fund or a BDC pursuant to the Names Rule cannot be changed unless authorized by the vote of a majority of the outstanding voting securities of the Fund. The Commission should adopt this amendment as proposed. The fundamental premise of the Names Rule is that a Fund that uses terms in its name suggesting a certain investment focus should be required to invest consistently with that focus. However, since unlisted closed-end funds and BDCs do not issue redeemable shares or list their shares on national exchanges, investors have little, if any, viable recourse or opportunity to leave a Fund if it seeks to change its 80% investment policy. A longer notice period would not solve this problem. The proposed amendment would ensure that shareholders have a voice in these decisions. Accordingly, NASAA encourages the Commission to adopt the amendment.

d. Conclusion as to the IC Names Proposal

A Fund's name is one of the earliest and most fundamental ways in which the Fund communicates with existing and potential investors. Investors rely on Fund names for valuable information about the Funds they choose to buy. When a Fund elects to use a name that suggests that it focuses its investments in a particular way, it is important that the Fund's name accurately reflect the Fund's investments. The IC Names Proposal would enhance discipline and clarity in Fund naming practices. Accordingly, NASAA supports its adoption.

II. The Disclosure Proposal Should be More Narrowly Tailored to Maximize its Potential Benefits.

The Disclosure Proposal would generally require both Funds and Advisers to make new, detailed disclosures about whether and how they consider ESG factors in their investment strategies. The depth and detail required in the proposed disclosure depends largely upon the degree to which the Fund or Adviser considers ESG factors. NASAA generally supports the Commission's objective to enhance and standardize disclosure by Funds and Advisers regarding their consideration of ESG factors in their investment strategies. However, we are concerned that the different categories in the Disclosure Proposal are insufficiently delineated, and that this shortcoming could result in excessive disclosure in edge cases where its value is less obvious. We are also concerned that this problem could blur the very distinctions that the Disclosure Proposal tries to draw and increase search costs for investors.

a. Compliance Burden on Smaller Advisers

There is significant variance in the sizes, business models, and resources of Advisers regulated by the states and the SEC. The Disclosure Proposal does not appear to adequately account for this fact, as it would impose similar requirements on all Advisers regardless of the compliance burden on the firm.[17] The Disclosure Proposal must strike the right balance between

[17] The Disclosure Proposal incorrectly states that "[the] proposed new rules and amendments would not affect most investment advisers that are small entities . . . because they are generally registered with one or more state

providing necessary and valuable information to investors and avoiding undue burdens on Funds and Advisers.

We encourage the Commission to revise the proposed amendments to Form ADV Part 2A to better tailor the disclosures based on the investment adviser's business practices and in recognition of the potential compliance costs. We suggest that the Commission reduce the prescriptive components, thereby easing the compliance burden on smaller Advisers to provide appropriate disclosure. Additionally, the Commission should limit the proposed disclosures, as described below, to Advisers who have affirmatively chosen to incorporate ESG factors as a significant or main consideration in their investment strategies, or who hold themselves out as incorporating ESG factors through their names, marketing materials, and other disclosures. We also encourage the Commission to consider other ways to mitigate the compliance burden on smaller advisers, such as a phase-in period for compliance. Appropriately tailoring the disclosures would benefit the Advisers required to comply with these provisions and the investors who rely on their advice. We would appreciate the opportunity to engage further with the Commission on how the how the disclosure requirements can be appropriately tailored.

If the Commission is unable or unwilling to more narrowly tailor the proposed disclosures, we request that the Commission further modify Form ADV Part 2A to state that the proposed disclosures in sub-Item 8.D. are mandatory for SEC-registered Advisers only. This would eliminate confusion for state-registered Advisers and allow state securities regulators to develop and implement an appropriate disclosure framework for state-registered Advisers.

b. "Integrated" and "Focused" Strategies

As an initial matter, the definition of an "integration" strategy is insufficiently clear to be operated effectively in practice. Critically, it is not clear what it means, in the context of the Disclosure Proposal, for a Fund or Adviser to have "consider[ed] one or more ESG factors." For instance, a Fund or Adviser could choose one issuer within its overall portfolio over a similarly-situated peer based on an ESG consideration, such as a demonstrated commitment to Board and management diversity or the company's exceptional treatment of its labor force. Yet that individual decision would likely have no material bearing on a Fund's focus overall. Furthermore, the Disclosure Proposal is unclear about whether this standard applies where a Fund or Adviser selects one investment over another based on an ESG factor, but does so primarily because of the effect that the ESG factor is likely to have on non-ESG dimensions of the company's performance.[18] We are concerned that the definition may be overinclusive, and that the proposed

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securities authorities and not with the Commission." Disclosure Proposal at 293. While it is true that SEC rules generally do not impose direct requirements on state-registered Advisers, the Disclosure Proposal would impose *de facto* requirements on these Advisers by requiring the proposed disclosures on a uniform form. *See*, *e.g.*, *NASAA Registration Requirements for Investment Advisers*, NASAA Model Rule 202(a)-1 (as amended Sept. 16, 2000), *available at* https://www.nasaa.org/wp-content/uploads/2011/07/13-IA202a1IARegisReqamend91600.pdf (requiring state-registered Advisers to complete, file, and amend Form ADV in accordance with its instructions). The Disclosure Proposal effectively disregards the potential impact of its proposed amendments on thousands of small- and mid-sized state-registered Advisers and the investors who rely on them.

[18] *See*, *e.g.*, Witold Henisz, Tim Koller, Robin Nuttall, McKinsey & Company, *Five ways that ESG creates value* (2019),

imposition of disclosure burdens on Funds and Advisers that neither purport nor attempt to engage in ESG-related focuses and strategies is unwarranted.

The Disclosure Proposal acknowledges, for example, that Funds and Advisers that engage in fundamental-oriented analysis have long considered governance factors in their investment selection processes, but the Proposal does not directly state whether these Funds or Advisers would be considered to fall within the "integration" category. We suspect that many or most of these Funds and Advisers would not consider themselves to be involved in "ESG" investing, nor would their investors or clients see them as such in any meaningful sense. Instead, such Funds or Advisers might simply say that ESG considerations are just discrete components in their thorough investment analyses. In our view, the likely result of this opacity is that industry practice will coalesce around plug-and-play, boilerplate disclosure language that provides meager practical value to investors. For example, Funds and Advisers may include disclosures that essentially restate the proposed definition of "integration" and likely including a statement that the Fund or Adviser does not consider greenhouse gas ("GHG") emissions in its analysis. These disclosures appear to be of relatively limited value to investors, particularly where ESG factors are not the intended direction of the strategy or an essential part of the investment thesis.

Accordingly, the scope of the Disclosure Proposal should be defined more tightly to target those Funds and Advisers for which ESG factors are a significant or main consideration in their strategies or who affirmatively hold themselves out as considering ESG factors (*i.e.*, "focused" strategies). This would help to ensure that disclosure is required where it is most needed. The investors for whom ESG-related disclosure is likely to be the most meaningful are unlikely to seek investment in a strategy in which ESG factors are "no more significant" than non-ESG factors. Tightening the scope in this manner would not free Funds or Advisers who meet the definition of "integration" from any disclosure related to their incorporation of ESG factors. In our view, the existing disclosure requirements in Forms ADV, N-1A, and N-2 are sufficient to encompass and require Funds and Advisers to provide much or all of the relatively limited disclosure proposed for "integration" strategies.[19] As such, it does not seem necessary to include "integration" strategies in the Disclosure Proposal.

Further, we note that, although the proposed disclosure requirements for Funds would expressly include within the "focused" definition those Funds whose names or marketing materials indicate a focus on ESG factors, there is no equivalent requirement for Advisers. The Commission should modify the Disclosure Proposal as it relates to Advisers to include within the definition of "focused" strategies any Adviser whose name, Form ADV Part 2A, or marketing materials indicate

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https://www.mckinsey.com/~/media/McKinsey/Business%20Functions/Strategy%20and%20Corporate%20Finance/Our%20Insights/Five%20ways%20that%20ESG%20creates%20value/Five-ways-that-ESG-creates-value.ashx (describing how "[g]etting your environmental, social, and governance (ESG) proposition right links to higher value creation").

[19] *See*, *e.g.*, Form ADV Part 2A, Item 8. (requiring Advisers to "describe the methods of analysis and investment strategies [the Adviser] use[s] in formulating investment advice or managing assets"); Form N-1A, Items 2 and 4 (requiring the disclosure of the Fund's investment objectives or goals and principal investment strategies); Form N-2, Item 24.4.g. (requiring disclosure of, *inter alia*, the investment strategies and techniques used by the Fund).

a focus on ESG factors. This change would help to ensure that Advisers who hold themselves out as focusing on ESG factors cannot evade disclosure or mislead investors by overstating their incorporation of ESG factors.

c. Greenhouse Gas Emissions Metrics

Although we generally support the Commission's goal of uniformity in GHG emissions disclosures for Funds that purport to use GHG emissions as a criterion in investment selection or engagement, we are concerned that the data for such disclosures may not be widely available for all potential holdings. Where the data is unavailable, Funds would be required to estimate, which may undermine the goal of uniformity and increase costs for investors.

We are also concerned that the proposed GHG emissions metrics might not adequately account for the rationale behind including certain portfolio companies in an ESG-"focused" Fund. For example, an electric vehicle manufacturer might have high GHG emissions, even though the downstream, long-term impacts of the investment might be fully in line with the Fund's objectives and strategy. Under similar circumstances, the disclosure of prescribed GHG emissions metrics may be misleading.

Finally, it is also possible that the prescribed metrics could become obsolete or stale in the future. We encourage the Commission to consider reframing the required GHG disclosure requirements as a principles-based requirements, rather than black-line rules. A principle-based approach would permit an appropriate degree of flexibility and is more likely to remain evergreen as circumstances change.

d. Disclosure of Proxy Voting Policies and Procedures

Notwithstanding our overarching concern about the burden and value of the proposed Adviser disclosures, NASAA supports the proposed amendment to Form ADV Part 2A, Item 17 regarding the voting of client securities. NASAA has consistently supported transparency in the context of proxy voting, particularly when someone has entrusted a third-party to vote on their behalf or advise them as to how they should vote.[20] The Disclosure Proposal would require an Adviser, who has specific voting policies or procedures to include one or more ESG considerations when voting client securities, to describe which ESG factors the Adviser considers and how the Adviser considers those factors. Clients deserve transparency into their Adviser's proxy voting policies and procedures. As such, NASAA supports this amendment.

e. Conclusion as to the Disclosure Proposal

NASAA is generally supportive of the goal to enhance and standardize ESG-related disclosures from Funds and Advisers who affirmatively undertake to include ESG factors in their overall strategies. However, we are concerned that the Disclosure Proposal is overinclusive and would result in excessive disclosure of questionable value for investors. Given the limited value

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[20] *See*, *e.g.*, Letter from Christopher Gerold, NASAA President (Feb. 3, 2020), https://www nasaa.org/wp-content/uploads/2020/02/NASAA-Comment-Letter-SEC-Releases-No-34-87457-34-87458-02-03-20.pdf.

of certain proposed disclosures, we are further concerned about the cost of such disclosure to smaller Advisers and to investors more broadly. Accordingly, we encourage the Commission to modify the Disclosure Proposal as described above before adoption.

III. Conclusion

NASAA supports the IC Names Proposal and encourages its adoption. However, NASAA is concerned about the scope of the Disclosure Proposal and encourages the Commission to modify it as described above. Thank you for considering these views. NASAA looks forward to continuing to work with the Commission in the shared mission to protect investors. Should you have questions, please contact either the undersigned or NASAA's General Counsel, Vince Martinez, at [redacted].

Sincerely,

Melanie Senter Lubin
NASAA President and
Maryland Securities Commissioner