

SECURITIES AND EXCHANGE COMMISSION

17 CFR Parts 270 and 274

[Release No. IC-36358; File No. S7-2026-36]

RIN 3235-AN45

Investment Company Cross Trading

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rule.

SUMMARY: The Securities and Exchange Commission (the “Commission”) is proposing to amend the rule under the Investment Company Act of 1940 (the “Investment Company Act”) that permits securities transactions between a registered investment company and certain affiliates (referred to as “cross trades”), subject to conditions. The proposed amendments are designed to expand the scope of securities that are eligible for cross trading, modernize the rule’s conditions, and enhance investor protection. The Commission also proposes to require aggregated reporting of trading activity and cross trades in Form N-PORT and Form N-MFP.

DATES: This proposal was published in the *Federal Register* on [INSERT DATE OF PUBLICATION IN THE *FEDERAL REGISTER*]. Comments should be received on or before [INSERT DATE 60 DAYS AFTER PUBLICATION IN THE *FEDERAL REGISTER*].

ADDRESSES: Comments may be submitted by any of the following methods:

Electronic Comments:

- Use the Commission’s internet comment form (<https://www.sec.gov/comments/s7-2026-36/investment-company-cross-trading>); or

- Send an email to rule-comments@sec.gov. Please include File Number S7-2026-36 on the subject line.

Paper Comments:

- Send paper comments to Vanessa A. Countryman, Secretary, Securities and Exchange Commission, 100 F Street NE, Washington, DC 20549-1090.

All submissions should refer to File Number S7-2026-36. This file number should be included on the subject line if email is used. To help the Commission process and review your comments more efficiently, please use only one method of submission. The Commission will post all comments on the Commission's website (<https://www.sec.gov/rules-regulations/public-comments/s7-2026-36>). Do not include personally identifiable information in submissions; you should submit only information that you wish to make publicly available. We may redact in part or withhold entirely from publication submitted material that is obscene or subject to copyright protection.

Studies, memoranda, or other substantive items may be added by the Commission or staff to the comment file during this rulemaking. A notification of the inclusion in the comment file of any such materials will be made available on the Commission's website. To ensure direct electronic receipt of such notifications, sign up through the "Stay Connected" option at www.sec.gov to receive notifications by email.

A summary of the proposal of not more than 100 words is posted on the Commission's website (<https://www.sec.gov/rules-regulations/2026/10/s7-2026-36>).

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SUPPLEMENTARY INFORMATION: The Commission is proposing for public comment amendments to 17 CFR 270.17a-7 (“rule 17a-7”), Form N-PORT (referenced in 17 CFR 274.150), and Form N-MFP (referenced in 17 CFR 274.201) under the Investment Company Act.

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I. INTRODUCTION

A. Overview

Section 17 of the Investment Company Act prohibits certain transactions with a registered investment company (a “registered fund”) by its “affiliated persons” and their “affiliated persons.”¹ Under section 17(a), an affiliated person of a registered fund, or an affiliated person of such a person, is generally prohibited from knowingly selling any security or

¹ See 15 U.S.C. 80a-17. Under section 2(a)(3) of the Investment Company Act, an “affiliated person” of a registered fund is generally defined to include: (1) directors, officers, employees, and the investment adviser; (2) any person owning 5% or more of the registered fund’s voting securities; (3) any person in which the registered fund owns 5% or more of the voting securities; and (4) any person directly or indirectly controlling, controlled by, or under common control with the registered fund. See 15 U.S.C. 80a-2(a)(3).

other property to, or purchasing any security or other property from, the registered fund when acting as a principal. This prohibition protects registered funds and their investors against overreaching or self-dealing by the registered fund's adviser, directors, and other affiliated persons by prohibiting affiliated transactions where one of the parties has both the ability and the pecuniary incentive to influence the actions of the investment company.²

These provisions, among other things, prohibit cross trades, that is, where a registered fund sells a portfolio investment to, or purchases a portfolio investment from, another fund or other person that is an affiliated person of the registered fund (or an affiliated person of such affiliated person).

In cases where there is no overreach, however, cross trades may benefit registered funds in several ways. For example, cross trades allow affiliated registered funds to avoid some of the costs associated with open market trades, such as brokerage commissions, bid-ask spreads, and other transaction expenses, when buying and selling securities with affiliated parties. Thus, section 17(b) of the Investment Company Act provides that the Commission shall issue exemptive orders to permit principal transactions with affiliates, including cross trades, when evidence establishes that certain criteria are satisfied. These criteria are:

- (1) The terms of the transaction, including the consideration paid and received, are reasonable and fair and do not involve overreaching;

² See, e.g., Investment Trusts and Investment Companies: Hearings on S. 3580 Before a Subcomm. of the Senate Comm. on Banking and Currency, 76th Cong., 3d Sess., at 256-59 (1940).

- (2) The transaction is consistent with each concerned registered fund's disclosed policies;
and
(3) The transaction is consistent with the general purposes of the Investment Company Act.³

To eliminate the need to file and process exemptive applications in situations where it appears likely that these statutory protections would be satisfied, the Commission adopted rule 17a-7 to permit cross trades of certain securities, subject to protective conditions that are based upon the requirements of section 17(b).⁴

Rule 17a-7 allows cross trades between a registered fund and certain of its affiliates (including affiliated registered funds and others who share a common investment adviser) ("eligible affiliates"), subject to the following conditions:⁵

- The security that is cross traded has readily available market quotations;
- The price of the cross trade is the independent current market price of the security as prescribed in the rule (for example, the last reported sale price of an exchange-listed security, or the average of the highest current independent bid and lowest current independent offer determined on the basis of reasonable inquiry if a security is traded over the counter);

³ See 15 U.S.C. 80a-17(b).

⁴ See Exemption of Certain Purchase or Sale Transactions Between Affiliated Registered Investment Companies, Investment Company Act Release No. 4697 (Sept. 8, 1966) [31 FR 12092 (Sept. 16, 1966)] ("1966 Adopting Release").

⁵ Eligible affiliates include an affiliated person of the registered fund, or an affiliated person of an affiliated person of the fund, that is: (1) another registered fund (including separate series); (2) another series of the same registered fund; or (3) another person whose affiliation is solely by reason of having a common investment adviser (or affiliated investment advisers), common directors, and/or common officers.

- There is no brokerage commission, fee (except customary transfer fees), or other remuneration paid in connection with the cross trade, and no consideration involved other than cash payment against prompt delivery of the security; and
- The cross trade is consistent with the policy of each registered fund participating in the trade.

Further, the rule places certain responsibilities upon a registered fund's board of directors (a "board") to adopt cross-trading procedures, oversee the registered fund's cross trades, and monitor potential conflicts. Specifically, the registered fund's board (including a majority of directors who are not interested persons of the registered fund) must adopt procedures reasonably designed to ensure that cross trades comply with rule 17a-7 and must approve changes to those procedures as the board deems necessary. The registered fund's board must also determine, no less frequently than quarterly, that all cross trades made during the preceding quarter complied with the procedures. The rule also requires the board to satisfy certain registered fund governance standards.⁶ Additionally, each participating registered fund must maintain certain records relating to its cross-trading procedures and transactions.

Separate from section 17(a) of the Investment Company Act, cross trading also involves considerations under the Investment Advisers Act of 1940 (the "Advisers Act"). Investment advisers have fiduciary duties to their clients, including registered funds, under the Advisers Act to serve the best interests of their clients and to seek best execution of a client's transactions.⁷ In

⁶ See 17 CFR 270.0-1(a)(7).

⁷ See, e.g., Commission Interpretation Regarding Standard of Conduct for Investment Advisers, Advisers Act Release No. 5248 (June 5, 2019) [84 FR 33669 (July 12, 2019)] ("Standard of Conduct Release").

addition, section 206(3) of the Advisers Act prohibits an investment adviser, directly or indirectly, from knowingly selling any security to or purchasing any security from a client without disclosing to the client the capacity in which the adviser is acting and obtaining the client's consent to the transaction.⁸ Rule 17a-7 currently does not provide exemptive relief from any provisions of the Advisers Act, and the proposed amendments likewise would not provide exemptive relief from these provisions. Compliance with rule 17a-7 also does not relieve a party engaging in a cross trade involving an Employee Retirement Income Security Act ("ERISA") plan from complying with applicable ERISA provisions.

Business development companies ("BDCs") are also subject to restrictions on affiliated transactions under section 57 of the Investment Company Act. Section 57 differs in some respects from the provisions for registered funds under section 17.⁹ Pursuant to section 57(i) of the Investment Company Act, until the Commission adopts rules for BDCs under section 57, BDCs are permitted to rely on rule 17a-7 to the extent that rule 17a-7 would permit a cross trade that section 57 would otherwise restrict. This release primarily focuses on the restrictions of section 17 of the Investment Company Act and therefore refers to registered funds throughout, but BDCs may rely on rule 17a-7 unless the Commission adopts BDC-specific rules under section 57 of the Investment Company Act in the future. The discussion in this release applies equally to BDCs.

⁸ 15 U.S.C. 80b-6(3).

⁹ For example, section 57 creates different categories of affiliated transactions and permits certain types of affiliated transactions if approved by both a majority of a BDC's directors or general partners who have no financial interest in the transaction and a majority of directors or general partners who are not interested persons of the BDC. 15 U.S.C. 80a-56.

B. Evolution of Funds' Cross-Trading Activities and Developments Underlying the Commission's Consideration of the Proposed Amendments

In 1966, when the Commission first adopted rule 17a-7, trades in equity securities were subject to substantial brokerage charges. The rule served the interests of investors by permitting affiliated funds to transact with each other, and thus avoid the payment of these brokerage charges, in situations where the Commission was likely to grant an exemption under section 17(b).¹⁰ As a result, Rule 17a-7 initially was limited to cross trades of equity securities that were traded on a national securities exchange and for which objective pricing information was available on the exchange.¹¹

In the early 1980s, recognizing that funds at that time increasingly invested in securities that traded over the counter but had an active trading market that generated independent pricing information, the Commission expanded the scope of rule 17a-7 to apply to trades involving any security for which market quotations are readily available.¹² The Commission did not define the term “readily available market quotations” at that time. Because the rule was no longer limited to equity securities, over time, registered funds came to rely on rule 17a-7 to cross trade fixed-income securities as well.

¹⁰ See 1966 Adopting Release, *supra* note 4.

¹¹ The Commission later amended the rule to include securities transactions entered into on a national inter-dealer quotation system that met certain conditions. See Exemption for Securities Traded in Over-the-Counter Market and Change in Annual Report Form N-1R, Investment Company Act Release No. 8494 (Sept. 13, 1974) [39 FR 36002 (Oct. 7, 1974)].

¹² See Exemption of Certain Purchase or Sale Transactions Between a Registered Investment Company and Certain Affiliated Persons Thereof, Investment Company Act Release No. 11676 (Mar. 10, 1981) [46 FR 17011 (Mar. 17, 1981)] (“1981 Adopting Release”).

When expanding rule 17a-7 to permit cross trades of over-the-counter securities, the Commission also amended the rule’s pricing provisions to require that these trades be priced at the average of the highest current independent bid and lowest current independent offer determined on the basis of reasonable inquiry. Historically, to meet this “reasonable inquiry” standard, registered funds obtained multiple bids and offers from broker-dealers for an over-the-counter security. In 1981, when the reasonable inquiry standard was adopted, quotes for fixed-income securities were generally obtained by calling individual broker-dealers on the phone.

Since that time, markets have undergone significant technological and structural changes, leading to pricing that is more verifiable, accessible, and transparent. For instance, fixed-income markets have seen developments in transparency, with Trade Reporting and Compliance Engine (TRACE) and Real-Time Transaction Reporting System (RTRS) reporting for many segments of the markets.¹³ In addition, there have been improvements in price discovery with the rise of electronic trading platforms, which can provide enhanced pre- and post-trade transparency. This includes, for example, systems that electronically display continuous trading interest (or “stream axes”) in a security or type of security on the system and “request for quote” (or “RFQ”) systems that are designed to allow market participants to obtain quotes for a particular security by sending messages to one or multiple potential respondents on the system simultaneously. Fixed-income exchange-traded funds (“ETFs”), which trade throughout the day and reflect what the

¹³ FINRA’s TRACE (introduced in 2002) is an over-the-counter real-time price dissemination service for eligible fixed-income securities, and MSRB’s RTRS has provided real-time information about transactions in municipal securities since 2005. See https://www.finra.org/sites/default/files/TRACE_Overview.pdf and <https://www.msrb.org/Market-Transparency-Programs>.

market believes to be the price of their underlying portfolios, also can serve as meaningful price discovery vehicles.¹⁴ Moreover, many registered funds engage third-party pricing services to provide pricing information.¹⁵ In the context of cross trading municipal securities, certain letters from the Division of Investment Management staff (“staff”) have addressed a fund’s use in cross trades of the price provided by an independent pricing service that values the fund’s municipal securities for purposes of determining the fund’s net asset value (“NAV”).¹⁶

The evolution of the registered fund industry in part drove increased demand to cross trade fixed-income securities. In the last twenty years, registered funds that invest primarily in fixed-income instruments have expanded from around \$1.5 trillion in assets to approximately \$7.9 trillion.¹⁷ Further, according to an industry survey, registered funds engaged in more than \$200 billion in cross trades of fixed-income securities in 2020 alone, resulting in estimated savings for those registered funds and their shareholders of over \$300 million.¹⁸

¹⁴ See, e.g., M. Tucker & S. Laipply, *Bond Market Price Discovery: Clarity Through the Lens of an Exchange*, 39 J. OF PORTFOLIO MGMT. 49 (2013).

¹⁵ See, e.g., Good Faith Determinations of Fair Value, Investment Company Act Release No. 34128 (Dec. 3, 2020) [86 FR 748 (Jan. 2, 2021)] (“Valuation Rule Adopting Release”), at section II.A.4.

¹⁶ See, e.g., United Municipal Bond Fund, SEC Staff No-Action Letter (Jan. 27, 1995) (“United No-Action Letter”); Federated Municipal Funds, SEC Staff No-Action Letter (Nov. 20, 2006) (“Federated No-Action Letter”). The statements in these letters and any other staff statements or guidance referenced in this release represent the views of Commission staff. Any such staff statements are not a rule, regulation, or statement of the Commission. Further, the Commission has neither approved nor disapproved their content. These statements, like all staff statements, have no legal force or effect, do not alter or amend applicable law, and create no new or additional obligations for any person.

¹⁷ See 2005 Investment Company Institute Fact Book, available at https://www.ici.org/doc-server/pdf%3A2005_factbook.pdf; 2026 Investment Company Factbook, available at <https://www.icifactbook.org/pdf/2026-factbook.pdf>.

¹⁸ See Letter of the Investment Company Institute (Apr. 9, 2021) (“ICI Letter”). The survey authors estimated that fixed income cross trading represents approximately 3.7% of the registered funds’ total fixed income trading activity. This letter was provided in response to a 2021 Commission staff statement on investment

In December 2020, the Commission adopted 17 CFR 270.2a-5 (“rule 2a-5”) under the Investment Company Act, which addresses fund valuation practices and the board’s role with respect to the fair value of a fund’s investments.¹⁹ Among other things, rule 2a-5 defines the term “readily available market quotations” because the requirement to determine a security or other asset’s fair value under the Investment Company Act and rule 2a-5 applies to securities and assets for which there are no readily available market quotations.

Rule 2a-5 provides that market quotations are readily available with respect to a security only when that “quotation is a quoted price (unadjusted) in active markets for identical investments that the fund can access at the measurement date, provided that a quotation will not be readily available if it is not reliable.”²⁰ This definition is consistent with the definition of a level 1 input in the fair value hierarchy outlined in U.S. generally accepted accounting principles (“GAAP”).²¹ However, this definition practically excludes most fixed-income securities from meeting the readily available market quotation standard because fixed-income securities trade infrequently and thus usually do not have active markets that provide the direct observable pricing inputs necessary to meet the standard.²²

company cross trading. *See infra* note 24. We discuss this survey and other information about the amount of registered funds’ cross-trading activities in different markets in more detail in section III.B.3.

¹⁹ See Valuation Rule Adopting Release, *supra* note 15.

²⁰ See rule 2a-5(c); Valuation Rule Adopting Release, *supra* note 15.

²¹ See Financial Accounting Standards Board Accounting Standards Codification (“ASC”) Topic 820-10-20. ASC Topic 820 categorizes inputs to valuation techniques used to measure fair value into three levels. The fair value hierarchy gives the highest priority to quoted, observable inputs (level 1) and the lowest priority to unobservable inputs (level 3).

²² We understand that most fixed-income securities are not level 1 securities for U.S. GAAP purposes but rather are typically classified as level 2 securities.

Because a security must have readily available market quotations to be eligible to be cross traded under current rule 17a-7, fixed-income securities that previously were cross traded under the rule prior to the adoption of rule 2a-5 generally have not been eligible for cross trading since September 8, 2022, the compliance date of rule 2a-5.²³ The Commission acknowledged in adopting rule 2a-5 that certain securities might become ineligible for cross trading under the new rule. The Commission also noted that consideration of amendments to rule 17a-7 was on its rulemaking agenda and welcomed input from the public as it considered potential revisions to the rule.

In March 2021, the staff issued a statement on investment company cross trading (the “Staff Statement”).²⁴ The Staff Statement noted that staff was assessing whether amendments to rule 17a-7 were warranted in light of the developments arising from the adoption of rule 2a-5 and the evolution of registered funds’ cross-trading practices over the last several decades, and solicited feedback on a number of relevant issues.²⁵ Response letters generally favored amending

²³ See Valuation Rule Adopting Release, *supra* note 15, at n.359 and accompanying text (“[t]he definition of readily available market quotations that we are adopting will apply in all contexts under the Investment Company Act and the rules thereunder, including rule 17a-7”). However, certain earlier letters by our staff address, among other things, the application of rule 17a-7 in the context of certain municipal securities transactions where there were no readily available market quotations. See, e.g., United No-Action Letter; Federated No-Action Letter. These letters were not withdrawn in connection with the adoption of rule 2a-5.

²⁴ See Division of Investment Management Staff Statement on Investment Company Cross Trading (Mar. 11, 2021), available at <https://www.sec.gov/newsroom/speeches-statements/investment-management-statement-investment-company-cross-trading-031121>. Unless otherwise indicated, letters cited in this release are the public responses to the Staff Statement, which are available at <https://www.sec.gov/investment/engaging-investment-company-cross-trading>. In this release, we generally refer to these public responses as “letters” or “response letters,” and we generally refer to the members of the public submitting the letters as “respondents.”

²⁵ Specifically, the Staff Statement sought feedback on: (1) registered funds’ current cross-trading practices; (2) pricing and liquidity requirements relating to determining the eligibility of securities to cross trade under rule 17a-7; (3) controls by registered funds and advisers relating to cross trading; and (4) issues relating to market transparency of cross trading.

rule 17a-7 to allow cross trading of fixed-income securities subject to protective conditions, while expressing differing views about the specifics of such conditions.

Members of the public have suggested other ways to improve cross trading of fixed-income securities beyond issues relating to the adoption of rule 2a-5. For example, some response letters suggested that rule 17a-7's pricing conditions, which for fixed-income securities require obtaining multiple bids and offers from broker-dealers who will not execute the transaction, should not be the sole permissible method of pricing such cross trades and presented challenges at times.²⁶ Similarly, the Fixed Income Market Structure Advisory Committee ("FIMSAC") issued recommendations in 2020 related to investment company cross trading.²⁷ FIMSAC's recommendations (which discussed cross trading prior to the changes brought about by rule 2a-5's adoption) suggested expanding rule 17a-7's pricing conditions for cross trades of fixed-income securities meeting the definition of a level 1 or level 2 security under GAAP to allow, for example, the use of independent pricing sources like those used to determine a registered fund's NAV.²⁸

²⁶ See, e.g., Letter of MarketAxess (Apr. 9, 2021) ("MarketAxess Letter"); Letter of the Securities Industry Financial Markets Association Asset Management Group (Apr. 12, 2021) ("SIFMA AMG Letter") (stating that obtaining bids and offers for certain fixed-income securities had become difficult, if not impossible, for funds due to a reduced willingness on the part of dealers to provide such market pricing information); Letter of T. Rowe Price (Apr. 14, 2021) ("T. Rowe Letter").

²⁷ See FIMSAC Recommendation Regarding Modernizing Rule 17a-7 under the 1940 Act (June 1, 2020) ("FIMSAC Recommendations"), available at <https://www.sec.gov/spotlight/fixed-income-advisory-committee/fimsac-recommendation-internal-fund-cross.pdf>.

²⁸ See FIMSAC Recommendations. FIMSAC also advocated for the use of electronic trading platforms to determine pricing, subject to certain protective conditions.

Respondents also suggested that rule 17a-7's requirements regarding conflict oversight, and the role that registered fund boards play in that oversight, deserve renewed attention.²⁹ For example, the rule's requirement that a registered fund's board review the fund's cross trades on a quarterly basis predates the enhancements to registered fund compliance programs mandated by 17 CFR 270.38a-1 ("rule 38a-1") which, among other things, placed responsibilities for administering a registered fund's compliance policies and procedures upon the fund's chief compliance officer ("CCO"). Consistent with rule 38a-1, in 2018, the staff stated that it would not recommend enforcement action to the Commission if a registered fund's board receives a written representation from the fund's CCO that transactions effected in reliance on rule 17a-7 complied with the procedures adopted by the board, instead of the board itself determining such compliance.³⁰ A number of respondents suggested that the Commission amend rule 17a-7 to formally relieve boards of the responsibility for reviewing transaction-specific cross-trading information and instead require procedures whereby boards periodically review and analyze reports from registered fund CCOs.³¹ Some also suggested that, if the Commission expands the scope of securities and pricing methods for cross trades, it could also consider requirements related to policies and procedures, post-trade forensic testing, and board or CCO oversight as sufficiently protective measures.³²

²⁹ See, e.g., Letter of the Investment Adviser Association (Apr. 11, 2021) ("IAA Letter").

³⁰ See Independent Directors Council, SEC Staff No-Action Letter (Oct. 12, 2018) ("IDC No-Action Letter"). This no-action position also applied to similar requirements in 17 CFR 270.10f-3 and 17 CFR 270.17e-1.

³¹ See, e.g., ICI Letter; T. Rowe Letter.

³² See, e.g., FIMSAC Recommendations; ICI Letter; SIFMA AMG Letter.

Some respondents and FIMSAC also suggested expressly allowing registered funds to pay certain fees in connection with effecting cross trades, such as custodial fees related to transferring securities or fees charged by an electronic trading platform for effecting a cross trade.³³ In addition, market participants have expressed different views related to the transparency and reporting of cross-trading activity.³⁴

C. Current Cross Trading Considerations

While markets have changed significantly since the Commission first adopted rule 17a-7 in 1966, response letters to the Staff Statement identify benefits that cross trades continue to offer to registered funds and their investors. For example, cross trading can help a registered fund avoid transaction costs that it would otherwise incur in open market transactions and counterparty risks.³⁵ Cross trading also can help a registered fund avoid market impacts, including price movement and price uncertainty, if the registered fund seeks to increase or reduce a position that is large enough to move the price of that security, and can provide greater execution speed and certainty relative to open market transactions.

Apart from potential benefits in transaction costs and pricing, cross trades can provide registered funds access to difficult to obtain securities that an advisory client might otherwise sell into the market due to redemption activity or other portfolio management considerations. Cross

³³ See, e.g., SIFMA AMG Letter; Letter of Wellington Management Company LLP (Apr. 12, 2021) (“Wellington Letter”); FIMSAC Recommendations.

³⁴ See, e.g., SIFMA AMG Letter; FIMSAC Recommendations; Letter of Dimensional Fund Advisors LP (Apr. 21, 2021) (“Dimensional Letter”).

³⁵ See, e.g., ICI Letter; Wellington Letter; SIFMA AMG Letter. For example, if a bond is trading on the open market with a bid of \$100.00 and an ask of \$100.50, then a selling fund would receive \$100.00 for the bond in the open market, while a buying fund would pay \$100.50 for the bond. If the funds instead cross traded the bond, they could transact at the midpoint price of \$100.25 and each realize a benefit of \$0.25.

trading also can provide an alternative source of liquidity for a selling registered fund where an affiliated fund or other account would benefit from purchasing the security in the cross trade, which can be an important benefit if few broker-dealers maintain an inventory of the security. Because of these benefits, it continues to be an appropriate use of our authority under sections 6(c) and 17(b) of the Investment Company Act to exempt cross-trading activity, subject to appropriate controls to prevent abuse or overreach.³⁶

While cross trades can provide significant benefits, cross trades also can implicate conflicts of interest in that an adviser may have the incentive, and ability, to favor one client over another to achieve higher advisory fees or other benefits for the adviser. These conflicts can lead to a registered fund being disadvantaged by its adviser in favor of higher-fee paying clients or other accounts, particularly when a security or other instrument is thinly traded. Examples of possible cross-trading abuses include:

- “Parking,” where an adviser may pre-arrange a cross trade with the intent to purchase the securities back at prices that disadvantage clients and evade regulatory oversight.³⁷

³⁶ Under section 6(c) of the Investment Company Act, the Commission may by rule, regulation, or order exempt any person or transaction or any class of persons or transactions from any provision of the Act if and to the extent that such exemption is necessary or appropriate in the public interest and consistent with protection of investors and the purposes fairly intended by the policy and provisions of the Act. *See* 15 U.S.C. 80a-6(c).

³⁷ *See, e.g.,* In the Matter of Morgan Stanley Investment Management Inc. and Sheila Huang, Investment Company Act Release No. 31947 (Dec. 22, 2015) (settled enforcement action alleging that a portfolio manager prearranged trades between affiliates at prices that favored certain clients over others and effected such trades through a broker-dealer to evade the firm’s internal cross-trade procedures); In the Matter of Western Asset Management Co., Investment Company Act Release No. 30893 (Jan. 27, 2014) (settled enforcement action alleging engagement in dealer-interposed cross trades at prices that favored one side over another).

- “Cherry-picking,” where more desirable investments are cross traded to a favored or more profitable client.³⁸
- “Dumping” where less desirable investments are cross traded to a less favored client.³⁹

As a result, cross trading must be subject to appropriate conditions, and registered funds must have effective and robust oversight mechanisms to guard against these potential conflicts.

Cross trading also has the potential to negatively affect price discovery and market integrity if large volumes of trades occur between affiliated parties. Unlike open market transactions, information about individual cross trades, such as the price, size, and instrument involved in the trade, generally is not publicly reported. The lack of transparency about the prices at which cross trades are effected may negatively affect the market’s price discovery processes. Similarly, the lack of information about the volume of cross trades may distort perceptions of the liquidity of a particular asset class or market. The lack of cross-trade information may reduce the broader market’s ability to accurately assess the value of certain securities or asset classes. As a result, some degree of transparency about funds’ cross-trading activities is necessary.

³⁸ See, e.g., In the Matter of SeaCrest Wealth Management, LLC, Advisers Act Release No. 6788 (Dec. 12, 2024) (settled enforcement action alleging that block trades were allocated among client accounts in a manner that favored some accounts over others).

³⁹ See, e.g., In the Matter of Macquarie Investment Management Business Trust, Investment Company Act Release No. 35325 (Sept. 19, 2024) (settled enforcement action alleging internal and dealer-interposed cross trades that were executed at prices that deviated from current market prices, causing certain purchasing accounts (primarily registered funds) to absorb trading losses that otherwise would have been borne by the selling unregistered pooled investment vehicles).

D. Overview of Proposal

We propose to modernize and expand rule 17a-7 to better allow cross trades that are beneficial to registered funds and their shareholders, while also updating the rule's conditions to ensure effective investor protection:⁴⁰

- *Expand securities eligible to be cross traded.* We propose to expand the types of securities eligible for trading under the rule to include securities that the registered fund values based on inputs that are observable, either directly or indirectly. This change would permit cross trading of most fixed-income securities under the proposed rule because observable inputs are available for most fixed-income securities. The proposed change would limit the universe of securities eligible for trading under the rule to securities that have an independent basis for pricing, including those with readily available market quotations and observable inputs, to reduce the risk of subjectivity, bias, or error in determining the price of the cross trade.
- *Updated pricing conditions.* Recognizing the current pricing conditions may not be well suited to modern markets, we propose to update the pricing conditions of the rule to require the cross trade be effected using one of two pricing methods, which would be considered the independent current market price for purposes of the rule. The first pricing method would use the value of the security determined in the registered fund's next computation of NAV. Under the second method, the cross trade would be effected

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The exemptions proposed would be necessary and appropriate in the public interest and consistent with the protection of investors and the purposes fairly intended by the policy and provisions of the Investment Company Act.

at a price that the registered fund's investment adviser determines reasonably represents the current market price for the security using one or more unaffiliated pricing sources. If the registered fund uses the second method, the fund's investment adviser would be required to periodically review the reasonableness of these prices.

- *Conflict oversight and recordkeeping.* In lieu of the rule's current board oversight requirements, the proposal would make a number of changes to the current rule designed to enhance investor protection and allocate oversight responsibility in an effective manner. In the first instance, the registered fund's adviser would be required to determine prior to effecting a transaction that the proposed cross trade is in the best interest of the fund. Additionally, the registered fund's CCO would be required to perform quarterly reviews of cross trades to determine compliance with the rule and report the results to the fund's board. The CCO would also be required to conduct at least annual back testing of cross trades, which must include analyses of the ultimate prices realized when any security purchased by a fund through a cross trade is ultimately sold, to look for patterns suggesting disadvantages to the fund relative to affiliates and report the results to the board. Funds would be required to maintain and preserve records of each cross trade, the information and material used by the CCO to make the required determinations (including the information and material used to determine at least quarterly whether the conditions of the rule were satisfied for each cross trade and for the at least annual disposition-based and other back-testing to identify potential abuses), and reports provided to the board.

- *Reporting.* Registered funds do not currently report information about their cross trades in a structured way. Additional reporting about a fund's cross-trading activity in the context of its overall trading activity would help investors, the Commission, and other market participants better understand the scope and breadth of cross-trading activities and how these activities relate to, and affect, other reported market information. The proposal would add requirements for registered funds that engage in cross-trading activities to report - on Form N-PORT and Form N-MFP - aggregate information, by asset class, about the value of securities a registered fund traded during the preceding month and corresponding information about cross-trading activity by asset class.
- *Other modernizations.* The proposed rule 17a-7 amendments would also expressly permit *de minimis* payments to unaffiliated parties for services such as clearing, settlement, and custody. In addition, the proposed amendments would provide that a cross trade must be consistent with the registered fund's policies and investment strategies. For clarity, we also propose to add defined terms to the rule related to the registered funds that may rely on the rule and the eligible affiliates with which they may cross trade. The proposed defined terms would not modify these aspects of the current rule.

II. DISCUSSION

A. Eligible Securities Expansion

We propose to amend rule 17a-7 to expand the scope of securities that are eligible to be cross traded under the rule. The proposed amendments would permit cross trading of securities that would be valued by a registered fund based on inputs that are observable, either directly or

indirectly, in addition to those with readily available market quotations.⁴¹ By expanding the eligible securities for funds to cross trade to include those with observable inputs, the proposal is designed to expand the benefits of cross trading to more transactions while protecting investors by ensuring that there is an independent basis for determining the price of the security.

Rule 17a-7 currently restricts the scope of securities that are eligible to be cross traded to securities for which market quotations are readily available.⁴² In 1981, when the Commission amended the rule to include this condition, the Commission stated that reliance on readily available market quotations provides an independent basis for determining that the terms of the transaction are fair and reasonable to each participating registered fund and do not involve overreaching.⁴³ The Commission further stated that this condition would limit cross trading to securities that trade in active secondary markets, making the securities more likely to have independent pricing information available.⁴⁴

Rule 2a-5 under the Investment Company Act, which the Commission adopted in 2020, defines readily available market quotations to mean that there is a quoted price (unadjusted) in active markets for identical investments that the fund can access at the measurement date, provided that a quotation will not be readily available if it is not reliable.⁴⁵ This definition is consistent with the definition of a “level 1” input in the fair value hierarchy outlined in U.S.

⁴¹ See proposed rule 17a-7(b)(1).

⁴² See current rule 17a-7(a).

⁴³ See 1981 Adopting Release, *supra* note 12.

⁴⁴ *Id.*

⁴⁵ See rule 2a-5(c).

GAAP.⁴⁶ A security is considered to have readily available market quotations if its value is determined solely by reference to level 1 inputs.⁴⁷ Under the proposed rule 17a-7 amendments, funds would continue to be allowed to cross trade securities that have readily available market quotations as defined in rule 2a-5 (*i.e.*, level 1 securities).

We understand that most fixed-income securities that registered funds seek to trade do not have readily available market quotations because, among other reasons, they are not frequently traded in the secondary market and therefore are not valued solely by reference to level 1 inputs. As discussed above, such securities generally have not been eligible to cross trade since the compliance date for rule 2a-5.⁴⁸ The Commission also understands that cross trading fixed-income securities could provide benefits to registered funds and registered fund shareholders, including, for example, lower transaction costs and access to difficult to obtain securities.⁴⁹

To recognize those benefits while still protecting investors, we propose to expand the scope of securities that are eligible to be cross traded under the rule to include securities that are valued by registered funds based on inputs that are observable, either directly or indirectly (“level 2 securities”). This proposed change – that a security valued based on direct or indirect

⁴⁶ See Valuation Rule Adopting Release, *supra* note 15, at section II.D; ASC Topic 820-10-20.

⁴⁷ See *id.*, at paragraph accompanying n.336.

⁴⁸ See current rule 17a-7(a); *supra* note 23 and accompanying text.

⁴⁹ See, *e.g.*, Lina Han et. al., *Cross Trading in the Corporate Bond Market*, SMU Cox Sch. of Bus., Research Paper No. 25-15 (2025) (stating that registered funds may benefit from cross trading due to, among other things, the funds avoiding transaction costs and obtaining difficult to obtain bonds); ICI Letter (stating that amending rule 17a-7 to permit registered funds to cross trade fixed-income securities, subject to certain conditions, would benefit funds and investors by lowering transaction costs).

observable inputs would be eligible – is designed to be consistent with the current definition of a level 2 input in the fair value hierarchy outlined in U.S. GAAP.⁵⁰ Level 2 inputs include, for example, quoted prices for similar securities in active markets, quoted prices for identical or similar securities in non-active markets, and inputs other than quoted prices that are observable for the security, such as credit spreads or interest rates and yield curves that are observable at commonly quoted intervals.⁵¹ For purposes of the proposed rule, we would consider a security to be valued based on inputs that are observable, either directly or indirectly, only to the extent that level 2 inputs are the lowest level of inputs that are significant to the entire measurement.⁵²

Although level 2 securities do not have readily available market quotations like level 1 securities, they do have other observable inputs, such as quoted prices or prices for similar assets, that can be independently verified and often have multiple pricing sources available. Requiring observable pricing inputs for cross trading eligibility reduces the potential for overreaching of the registered fund by the adviser, and would increase the likelihood that the terms of a cross trade are fair and reasonable to each participating registered fund consistent with the provisions for exemptive relief under section 17(b) of the Investment Company Act. Therefore, we propose

⁵⁰ See ASC 820-10-20; ASC 820-10-35-47 (providing that level 2 inputs are inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly or indirectly). Observable inputs are those that are developed using market data, such as publicly available information about actual events or transactions, and that reflect the assumptions that market participants would use when pricing the security. See ASC 820-10-20 (defining “observable inputs”).

⁵¹ See ASC 820-10-35-48.

⁵² See ASC 820-10-35-37A (providing that where the inputs used to measure the fair value of an asset or liability are categorized within different levels of the fair value hierarchy, the fair value measurement is categorized in its entirety in the same level of the fair value hierarchy as the lowest level of input that is significant to the entire measurement).

to expand the scope of securities that are eligible to be cross traded to include securities that would be valued by the registered fund based on inputs that are observable, either directly or indirectly, which we understand would include many fixed-income securities.⁵³

Securities valued based on unobservable inputs that are significant to the entire measurement (*i.e.*, “level 3” inputs under U.S. GAAP) or that are non-leveled under U.S. GAAP (*i.e.*, investments that are not categorized within the fair value hierarchy, certain private fund-issued securities that are valued using those private fund shares’ NAV as a practical expedient) would *not* be eligible for cross trading under the proposal.⁵⁴ Given the conflicts of interest implicated by cross trades and the importance of the transaction price to ensure that a cross trade is fair and reasonable to each participating registered fund and does not involve overreaching, we propose to permit cross trading under rule 17a-7 only of securities corresponding to assets whose fair value measurement is categorized as level 1 or level 2 within the current U.S. GAAP fair value hierarchy.⁵⁵ The proposed approach is designed to focus on securities that have an independent basis for pricing, including those with readily available market quotations and

⁵³ According to an industry survey, 99.6% of the fixed-income securities that funds that responded to the survey cross traded in 2020 were classified as level 2 securities. *See* ICI Letter.

⁵⁴ *See, e.g.*, ASC 820-10-35-51 (“An adjustment to a Level 2 input that is significant to the entire measurement might result in a fair value measurement categorized within Level 3 of the fair value hierarchy if the adjustment uses significant unobservable inputs”); ASC 820-10-15-4 through 15-5; ASC 820-10-35-59 through 35-62 (permitting a security that does not have a readily determinable fair value to be valued based on the issuer’s net asset value per share (or its equivalent) as a practical expedient under certain circumstances).

⁵⁵ Overall, registered funds’ holdings of level 3 investments are small in comparison to level 1 and level 2 investments. For example, based on a review of Form N-PORT filings as of February 2026, less than 1% of the total value of all reporting funds’ investments were in level 3 investments. Of the investments that funds reported as level 3, it was more common for investments in the loan, equity preferred, and real estate asset classes to be reported as level 3 than investments in other asset classes.

observable inputs, thus reducing the risk of subjectivity, bias, or error in determining the price of the cross trade.

These proposed amendments are designed to allow cross trading of securities that have an independent basis for pricing the trade as they are less likely to raise the same concerns regarding overreaching that rule 17a-7 was designed to address. This, in combination with the proposal's other conditions, are designed to expand the benefits of cross trading to more funds and shareholders while protecting investors from the conflicts of interest implicated by cross trades.

We request comment on the proposed eligible securities requirements.

1. Instead of expanding the rule to include level 2 securities, should we further broaden or narrow the scope of securities that are eligible for cross trading? If so, which securities should be eligible for cross trading, why, and under what circumstances? Do those securities have an independent basis for valuation and low risk of subjectivity, bias, or error in determining the price of a cross trade, thus making it more likely that the terms of the cross trade would be fair and reasonable to each participating fund?
2. If we allow funds to cross trade a broader scope of securities than proposed (*e.g.*, all or certain types of level 3 securities), should we include other conditions beyond those that we propose? Should those conditions apply to cross trades of all permitted securities, or only to certain types of securities? How would those conditions address the potential for overreaching or conflicts of interest when securities may lack an independent, observable basis for valuation? For example, should we require prior trade-by-trade board or board committee approval, including by a majority of directors who are not interested persons of the fund, for cross trades of securities that are not level 1 or level 2 securities, or

additional pricing, documentation, escalation, and post-trade review processes to verify pricing fairness for cross trades of such securities (*e.g.*, the cross-trade price must be aligned with the valuation determined for purposes of the fund's NAV, portfolio managers must obtain advance written approval from the fund's board or CCO to cross trade these securities, the fund must report details of these cross trades to the Commission or the public, or cross trades of these securities must be reviewed by the CCO and reported to the board more frequently than the quarterly reviews the proposal would require)?

3. Are there any types of securities that registered funds currently cross trade under rule 17a-7 that would no longer be eligible to cross trade under the proposed amendments to rule 17a-7?
4. Are there securities that would be included within the scope of the proposed eligibility conditions that commenters believe should not be eligible for cross trading? If so, which securities and why?
5. The proposed approach tracks concepts in current U.S. GAAP related to valuation. Should we use these concepts for defining the scope of eligible securities that registered funds can cross trade? Are there potential unintended consequences that could arise from linking the rule to concepts in current U.S. GAAP? Should we use a different approach to define the scope of eligible securities and, if so, what approach should we use for this purpose? For example, should the scope of eligible securities be based on asset class?
6. Rather than limit the scope of securities that registered funds can cross trade, should we permit funds to cross trade any security provided that other conditions of the rule are

met? If funds should be permitted to cross trade any security, please explain why other conditions in the rule would be sufficient to address overreaching and conflicts of interest or whether there are additional conditions that should apply to such cross trades.

B. Pricing of Cross Trades

We propose to amend rule 17a-7 to provide two alternative methods for pricing cross trades. Under the proposal, a cross trade would be effected at the independent current market price, which for purposes of rule 17a-7 would be either:

- (1) The value of the security determined in the registered fund's next net asset value computation on the business day of the cross trade ("NAV pricing"); or
- (2) A price that reasonably represents the current market price, as determined by the registered fund's adviser using one or more unaffiliated pricing sources ("current market pricing"), provided that the adviser periodically reviews the reasonableness of such prices.⁵⁶

The proposed pricing provisions are designed to recognize developments since the Commission last amended this aspect of the rule, including the availability of more verifiable, accessible, and transparent pricing information, and the adoption of rule 2a-5, which led to enhancements to the regulatory framework for fund valuations. The proposal is designed to help address conflicts of interest that could incentivize cross trading at a price that is more favorable to an eligible affiliate than to the registered fund.

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See proposed rule 17a-7(b)(2).

Rule 17a-7 currently prescribes different methods for determining the price of a cross trade, depending principally on whether the security is exchange listed or traded over the counter. For example, for most listed equity securities other than options, the price of the cross trade is the last sale price with respect to the security reported in the consolidated transaction reporting system or, if there are no reported transactions that day, the average of the highest current independent bid and lowest current independent offer for such security. For fixed-income securities and other securities traded over the counter, in contrast, the price of the cross trade is the average of the highest current independent bid and lowest current independent offer determined on the basis of reasonable inquiry.⁵⁷ As discussed above, prior to the adoption of rule 2a-5, registered funds cross traded some fixed-income securities. We understand that registered funds cross trading such securities generally satisfied the rule's pricing requirements by gathering multiple bids and offers from broker-dealers.⁵⁸

Several letters in response to the Staff Statement and other staff outreach addressed the rule's current pricing requirements, including feedback that the pricing provisions should be broader and more flexible. For example, some suggested that funds should be able to price cross trades using multiple inputs and sources of data, including independent evaluated prices and broker-dealer quotes.⁵⁹ Some supported use of independent pricing sources providing evaluated prices that are used for valuation purposes under rule 2a-5.⁶⁰ In light of this feedback, the

⁵⁷ See current rule 17a-7(b).

⁵⁸ See, e.g., United Municipal Bond Fund, SEC Staff No-Action Letter (July 30, 1992).

⁵⁹ See, e.g., ICI Letter; IAA Letter; Letter of Capital Group (May 6, 2021) ("Capital Group Letter").

⁶⁰ See, e.g., ICI Letter; Capital Group Letter; DFA Letter.

improvements in transparency and price discovery methods available, as well as the significant diversity in how different types of investments are priced, the pricing requirements of the proposed rule are designed to provide funds with the ability to price a cross trade flexibly and efficiently while maintaining investor protections. We also recognize that price discovery methods are likely to continue to evolve, and the proposed approach is intended to be dynamic rather than identifying particular pricing sources that funds must or may use.

In addition to proposing to expand the scope of securities eligible for cross trading by registered funds beyond those with readily available market quotations (level 1 securities) to also include securities valued based on directly or indirectly observable inputs (level 2 securities), we propose that each cross trade would be effected at the independent current market price determined using one of two pricing methodologies, either NAV pricing or current market pricing. A registered fund may switch between the two pricing methodologies for different cross trades. Pricing under the proposal would be subject to controls and oversight. If a fund uses NAV pricing for cross trades, the price of a cross trade would be subject to existing valuation processes and oversight procedures compliant with rule 2a-5 designed to ensure those prices are reasonable. If a fund uses current market pricing for cross trades, it would need to develop processes and oversight procedures to support the determination that the price reasonably represents the current market price and to comply with the proposed requirement for the adviser to periodically review the reasonableness of these prices. This approach is intended to address concerns respondents raised about the existing pricing provisions while promoting reasonable and fair pricing of cross trades. These pricing-specific conditions are designed to work with other

proposed controls and oversight to promote investor protection, such as the investment adviser's best interest determination.

1. NAV Pricing

We propose to amend rule 17a-7 to provide that a cross trade could be effected at the price determined by using NAV pricing. The transaction would be effected at the value the registered fund ascribes to the security in its next computation of the registered fund's current net asset value under section 2(a)(41) of the Investment Company Act and 17 CFR 270.2a-4 ("rule 2a-4") and rule 2a-5 on the business day on which the transaction occurs. By leveraging existing valuation processes that are already subject to robust controls and oversight, the NAV pricing approach is designed to be a cost-effective method of pricing cross trades that would limit the potential for abuses.

Under this proposed approach, the cross-trade price would be determined by the registered fund's next computation of its NAV on the business day of the cross trade. Many registered funds make NAV determinations at the close of business each day, and some funds—such as some money market funds and ETFs—make NAV determinations intra-day. Under the proposal, the registered fund would use the value determined in the next NAV computation on that day, whether it is at close of business or intra-day. Registered funds, such as some closed-end funds, that do not compute their NAVs on a daily basis would be permitted to use the NAV pricing approach only on days that their NAVs are computed. If a cross trade involves two registered funds, the registered funds must share the same valuation processes so that they would arrive at the same price using the NAV pricing approach. For registered funds that have valuation processes, such as the pricing sources used, that could result in different valuation

outcomes under the NAV pricing approach, the cross-trade price could only be determined under the current market pricing approach.

The NAV pricing approach would establish a standard that is consistent with the registered fund's valuation policies and procedures and that would apply to all types of securities that funds may cross trade, while allowing for differences in how various types of securities are priced. Specifically, when using NAV pricing, the cross-trade price would be either the current market value (in the case of securities with readily available market quotations) or the fair value (in the case of other securities and assets) based on observable inputs determined in the registered fund's next NAV computation.⁶¹

The proposed rule would not, however, permit use of the amortized cost value of a security that some money market funds are permitted to use for purposes of computing their NAVs under 17 CFR 270.2a-7 ("rule 2a-7"). An amortized cost method of valuation values portfolio securities at their acquisition cost as adjusted for amortization of premium or accretion of discount, rather than valuing securities based on current market factors. Current rule 17a-7 requires cross trades to be effected at the "current market price," and our proposed amendments similarly focus on market-based pricing. Money market funds that use the amortized cost method of valuation are separately required to calculate their NAVs using available market quotations (or an appropriate substitute that reflects current market conditions) at least daily, and they could use those NAV prices under the proposed NAV pricing approach.⁶²

⁶¹ See section 2(a)(41) under the Investment Company Act; 17 CFR 270.2a-4; 17 CFR 270.2a-5.

⁶² See 17 CFR 270.2a-7(g)(1).

Registered funds relying on this approach would use the same pricing methodologies to determine the cross-trade price as they use for fund valuations. A fund would not be required to determine the cross-trade price separately, which should result in an efficient and cost-effective pricing process. This approach is designed to allow many cross trades to leverage existing processes.

We propose the NAV pricing approach because it utilizes an existing methodology with robust processes, subject to rule 2a-5, to determine the price for the cross trade. These processes and controls would decrease the likelihood of inappropriate values for cross trading purposes and help address conflicts of interest while preserving the benefits of cross trading, such as reduced execution costs. Further, because NAV pricing is derived from a fund's own valuation processes, which are themselves already subject to significant board oversight and scrutiny, this pricing method benefits from the same rigor and independence that governs the fund's broader valuation framework.⁶³ This is expected to provide an additional layer of protection against conflicts of interest that can incentivize pricing a cross trade to the disadvantage of the registered fund and its shareholders relative to the eligible affiliate. In addition, because NAV pricing relies on the fund's valuation processes, we would expect any improvements to valuation techniques to apply to NAV pricing, which would improve cross trade pricing over time.

⁶³ See, e.g., Valuation Rule Adopting Release, *supra* note 15, at nn.191-220 and accompanying text (outlining guidance on board oversight of the valuation process).

2. Current Market Pricing

Additionally, we propose to amend rule 17a-7 to provide that a cross trade could be effected at a price determined by the registered fund's investment adviser to reasonably represent current market price for the security using one or more unaffiliated pricing sources, provided that the adviser periodically reviews the reasonableness of such prices.⁶⁴ Similar to the valuation process underlying NAV pricing, current market pricing may take into account multiple inputs and sources of data. Additionally, current market pricing may be used at any time, including intra-day, unlike NAV pricing, which would be determined by the registered fund's next computation of its NAV on the business day of the cross trade. The adviser, in using any unaffiliated pricing source, first would need to determine that the price reasonably represents the current market price for the security and also would need to periodically review the reasonableness of the prices used under this provision.

We understand that it is not always practical or possible for registered funds to use NAV pricing to price cross trades. For example, a registered fund may wish to effect a cross trade intra-day, before the fund's next NAV computation, which is often at the close of business. Additionally, to analyze compliance with the rule's conditions, an adviser may find it more efficient to have all information about the potential cross trade, including pricing information, available at the time of the trade decision, instead of waiting for an end of day valuation process to be completed. As another example, for registered funds that do not compute their NAVs on a daily basis (*e.g.*, some closed-end funds), a registered fund may wish to effect a cross trade on a

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Proposed rule 17a-7(b)(2)(ii).

day on which the fund will not compute its NAV. Using the current market pricing approach, the adviser might reasonably determine that using the same valuation methodology for the security as the fund would use if it were computing its NAV on that day would reasonably represent the current market price for the security.⁶⁵ In these and other situations, allowing a registered fund's investment adviser to determine a cross-trade price that reasonably represents the current market price for the security using unaffiliated pricing sources would further promote the cost-saving benefits of cross trading while helping address conflicts of interest.

Determination that a Price Reasonably Represents the Current Market Price

Using the proposed current market pricing approach, the registered fund's investment adviser would be required to determine the price that reasonably represents the current market price for the security being cross traded using one or more unaffiliated pricing sources. Consistent with funds' valuation methodologies and the current pricing provisions in rule 17a-7, the adviser's analysis of current market price and sources for unaffiliated pricing information would generally vary by asset type. A security with readily available market quotations must have quoted prices in active markets that the registered fund can access and that are reliable.⁶⁶ For these securities, the adviser should look to the prices at which a particular security is being traded and quoted in active markets to determine a price that reasonably represents the current market price. For example, for cross trades of listed equity securities, it generally would be appropriate to use either the last reported sale price or, if there are no reported transactions on

⁶⁵ The registered fund, however, would not be required to value each of the securities in the registered fund or determine NAV for the registered fund in order to determine the price for the particular security being cross traded.

⁶⁶ See rule 2a-5(c).

that day, the average of the highest current independent bid and the lowest current independent offer. This would be consistent with the current rule's asset-specific pricing requirements.

Although we propose to remove these asset-specific pricing requirements in favor of standards that can be applied across permissible asset types, we do not intend for the proposed amendments to change how funds price cross trades of listed equity securities with readily available market quotations and continue to view the current rule's requirements as an appropriate way to comply with the proposal.

For securities that do not have readily available market quotations, a registered fund's investment adviser would use observable inputs from one or more unaffiliated pricing sources to determine a price that reasonably represents the current market price for the security. Registered funds already use various unaffiliated pricing sources, such as pricing services that provide evaluated prices by using matrix or model-based pricing methodologies, to support their NAV determinations. Broker-dealer quotes may continue to provide valuable pricing inputs. In addition, newer and developing sources, such as electronic trading platforms, may provide observable inputs to help determine price for some asset types, and we also understand that some pricing services are offering intra-day evaluated prices. These available unaffiliated pricing sources may be used by a registered fund's investment adviser to determine a price that reasonably represents the current market price for a cross trade. The proposal would also allow developing technologies and new unaffiliated pricing sources to be used.

Under the proposal, the pricing sources an investment adviser uses would need to be unaffiliated. The proposed rule would define "unaffiliated" to be a person other than an affiliated person or promoter of, or principal underwriter for, a fund (*e.g.*, a first-tier affiliate) or an

affiliated person of such entities (*e.g.*, a second tier affiliate), consistent with the coverage of section 17(a).⁶⁷ Requiring the pricing sources to be unaffiliated reduces the potential for conflicts of interest between the registered fund and the adviser and is designed to increase the likelihood that the terms of a cross trade are fair and reasonable to each participant and do not involve overreaching, consistent with section 17(b) of the Investment Company Act. The current rule similarly provides that cross trades must be effected at the independent current market price.⁶⁸

Regardless of the type of security or the unaffiliated pricing source used, the proposal would require the adviser to make a determination that the price of the cross trade reasonably represents the current market price for the security. There are different ways an adviser might make this determination before executing a cross trade, and the approach may vary based on the type of security or the unaffiliated pricing source used. For example, an investment adviser considering the use of broker-dealer quotes as an unaffiliated pricing source generally should confirm with more than one broker-dealer that the quotes reflect current market conditions, are timely, are binding, and are verifiable (based on real transactions or other similar available quotes). These and any other appropriate factors would help inform an adviser's consideration of whether an average price based on the highest bid and lowest offer from the broker-dealers reasonably represents the current market price for the security. "Indications of interest" or "accommodation quotes" (*i.e.*, non-firm expressions of interest to trade at a given price) would

⁶⁷ See proposed rule 17a-7(d).

⁶⁸ See current rule 17a-7(b).

not reasonably represent the current market price of a security for purposes of cross trades under proposed rule 17a-7.⁶⁹

Similarly, an investment adviser considering the use of prices from a pricing service as an unaffiliated pricing source, including for intra-day evaluated prices for securities that do not have readily available market quotations, should conduct due diligence on the service and its methodologies to determine whether prices provided by the service can be reasonably determined to represent current market value for the security. In this due diligence, an adviser could consider factors such as:

- The qualifications, experience, and history of the pricing service, particularly in providing intra-day pricing;
- The pricing methods or techniques, inputs, and assumptions the pricing service uses for different classes of holdings, how they are affected (if at all) as market conditions change, and, if the same pricing service is used for both NAV computation and current market pricing, how these methods or techniques may differ;
- The quality of the pricing information the service provides and the timing of the service's determination of pricing information relative to the timing of the cross trade;
- The pricing service's process for considering pricing challenges, including how the pricing service incorporates information received from pricing challenges into its pricing information;

⁶⁹ This is consistent with prior Commission statements related to current rule 17a-7. *See* Investment Company Liquidity Risk Management Programs, Investment Company Act Release No. 32315 (Oct. 13, 2016) [81 FR 82142 (Nov. 18, 2016)] (“Liquidity Rule Adopting Release”) at nn.800-801 and accompanying text.

- The pricing service’s actual and potential conflicts of interest (*e.g.*, potential conflicts associated with maintaining continuing business relationships and the potential incentive to provide higher or more aggressive prices to retain business) and the steps the pricing service takes to mitigate such conflicts; and
- The testing processes the pricing service uses, especially for newer technologies such as intra-day pricing information.⁷⁰

Allowing registered funds’ investment advisers to determine cross-trade prices that reasonably represent current market prices using unaffiliated pricing sources such as pricing services and broker-dealer quotes is consistent with allowing registered funds to use these sources as part of a registered fund’s NAV computation. In addition, improvements to the pricing process as a result of the adviser’s evaluation of current market price could improve the NAV computation process.⁷¹ Similar to registered funds’ valuation considerations, a registered fund relying on the current market pricing approach should select and apply in a consistent manner the methodologies the adviser uses to determine a price that reasonably represents the current market price.⁷² To the extent a fund uses the same pricing source for both NAV computation and current

⁷⁰ See Valuation Rule Adopting Release, *supra* note 15, at paragraph accompanying n.117 (discussing similar factors for consideration when using pricing information provided by a pricing service in determining the fair values of the fund’s investments).

⁷¹ The current market price may also be used as an input to a fair value measurement if the fund has evidence that the transaction was entered into at market terms. See Financial Accounting Standards Board (FASB), Master Glossary: Market Participant, at <https://asc.fasb.org/MasterGlossary>.

⁷² See rule 2a-5(a)(2) (requiring that, for purposes of fair value determinations, a registered fund select and apply in a consistent manner an appropriate methodology or methodologies for determining (and calculating) the fair value of fund investments, provided that a selected methodology may be changed if a different methodology is equally or more representative of the fair value of fund investments, including specifying the key inputs and assumptions specific to each asset class or portfolio holding).

market pricing, it may combine the due diligence on the same vendor for both purposes and would not need to conduct a separate due diligence process.

Reviewing the Reasonableness of Prices

Under the proposed current market pricing approach, the registered fund's investment adviser would be required to periodically review the reasonableness of the prices. This review requirement is designed to ensure that prices determined under the current market pricing approach are reasonable and subject to appropriate oversight through periodic reviews.

We are not proposing to require a particular method of reviewing cross-trade prices determined using the current market pricing approach or the frequency at which these reviews must occur. The investment adviser's review of the prices determined under the current market pricing approach for reasonableness would be established by the investment adviser and should be specific to the circumstances of the registered fund's cross trading, the type of security being cross traded, and the frequency and volume of cross-trading activity.

When structuring the method and frequency of reviewing cross-trade prices under the current market pricing approach, it would be reasonable to consider the methods for reviewing a fund's valuations for purposes of NAV computations and whether applying such methods (or similar methods) would be appropriate for these purposes. For example, under rule 2a-5, funds must periodically review the appropriateness and accuracy of the fair value methodologies selected and make any necessary changes or adjustments to them, test the appropriateness and accuracy of fair value methodologies, and evaluate pricing services if used.⁷³ These types of

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See rule 2a-5(a)(2)(ii), (3), and (4).

reviews could potentially be leveraged to review the reasonableness of prices used under the current market pricing approach. For example, if a specific approach to determining cross-trade prices consistently over- or under-prices securities as compared to observed market transactions or valuations used for NAV purposes, the adviser should investigate the reason for the difference and consider whether use of that approach for pricing cross trades continues to be reasonable.

Under the proposed rule, the registered fund's adviser would be responsible for conducting the periodic review of the reasonableness of prices used under the current market pricing approach. This review requirement would be separate from CCO review requirements in the proposal, which are more focused on reviewing cross trades for compliance with the rule, although the periodic reviews would be within the scope of the CCO's overall compliance assessments as well. We propose to require the adviser to conduct this pricing review because the adviser overall is better situated to review the reasonableness of cross-trade prices than fund CCOs, as these reviews would involve considerations about available market data, and the choice of and reliability of different pricing sources. In addition, the adviser may be able to react more accurately and quickly to correct pricing issues than the CCO. This review is similar to the reviews that advisers may conduct for purposes of fund valuations.

As discussed below, the proposed rule would require the retention of the information or materials upon which the CCO makes certain compliance-related determinations. This recordkeeping requirement would include information or materials used to determine that the pricing conditions of the proposed rule are satisfied.⁷⁴ These records are designed so that a CCO

⁷⁴ See proposed rule 17a-7(c)(2); see also *infra* section II.G (discussing the proposed recordkeeping requirements).

would have the necessary information to review whether and how the investment adviser determined that the price reasonably represents the current market price, as well as the periodic review of the reasonableness of prices.

We request comment on the proposed pricing requirements for cross trades.

7. Are the proposed methodologies for pricing cross trades workable in practice?
8. Would registered funds participating in cross trades receive a fair and reasonable independent current market price for the securities involved under the proposed pricing methodologies?
9. Should we permit registered funds to use either the NAV pricing approach or the current market pricing approach for a cross trade, as proposed? Should a registered fund be permitted to switch between one pricing methodology and another for different cross trades, as proposed? Are the proposed approaches sufficiently evergreen? Would these approaches have any issues in an extended trading hours environment? Are there other ongoing or reasonably anticipated market developments that may raise issues with the proposed approach?
10. Should we alternatively require cross trades to be priced under a single standard, or different standard(s) than those proposed? If so, would NAV pricing, current market pricing, or some other standard be most appropriate for a uniform approach? Should we permit more than two approaches to pricing? How would we ensure that investors are protected using those methods given the conflict of interest implicated by cross trading? What are the advantages and disadvantages to each method?

11. Do the NAV pricing approach and the current market pricing approach work for all assets that registered funds would be permitted to cross trade under rule 17a-7? Should we have more specific pricing provisions based on, for example: how a security is traded, like the current rule; asset type (*e.g.*, such as equities or fixed income, or level 1 or level 2 securities, to recognize differences in pricing sources); type of fund (*e.g.*, such as closed-end or open-end); or some other method? Commission staff no-action letters have addressed pricing cross trades for certain types of securities, including municipal securities and variable rate demand notes (“VRDNs”).⁷⁵ Are the proposed pricing provisions workable for these types of securities, or would registered funds need different conditions or guidance to facilitate pricing cross trades for these securities?
12. Are there circumstances in which either NAV pricing or current market pricing should not be permitted? For example, we understand that some registered funds value portfolio investments at the bid price, rather than the mid price, when computing their NAVs.⁷⁶ Rule 17a-7 currently requires that cross trades be executed at mid prices. Should registered funds that price at bid be permitted to cross trade at the bid price under NAV

⁷⁵ See, *e.g.*, Federated No-Action Letter (providing that the staff would not recommend enforcement action if cross trades of municipal securities that lack readily available market quotations are conducted at a price provided by an independent pricing service that values the fund’s municipal securities for purposes of determining the fund’s net asset value); Benham California Tax Free Trust and Benham National Tax-Free Trust, SEC Staff No-Action Letter (Aug. 6, 1986) (providing that the staff would not recommend enforcement action if cross trades of VRDNs are priced at par plus accrued interest).

⁷⁶ See ASC 820-10-35-36C. GAAP provides that if an asset measured at fair value has a bid price and an ask price (for example, an input from a dealer market), the price within the bid-ask spread that is most representative of fair value in the circumstances shall be used to measure fair value, and that the use of bid prices for asset positions is permitted but not required for these purposes. *Id.*; see also ASC-820-10-35-36D (stating that use of mid-market pricing as a practical expedient for fair value measurements within a bid-ask spread is not precluded). Mid-market pricing values a security at the average of its bid and ask prices. Since a seller generally asks for a higher price for a security than a buyer bids for that security, the mid-market price is higher than the bid price for a security, but lower than its ask price.

pricing when doing so aligns with the valuation of the security or should they use current market pricing? Is using NAV pricing at bid fair and reasonable for the seller in the cross trade, even though it is receiving a lower price than it would if mid prices were used?

What would be the advantages and disadvantages of allowing cross trades to occur at bid prices under the NAV pricing approach? For example, the seller would not avoid spread costs under these circumstances but might avoid other costs associated with open market transactions (*e.g.*, market impact) and experience reduced risks (*e.g.*, counterparty or liquidity risk).

13. Under the proposed NAV pricing approach, the execution price for a cross trade would not be known until the registered fund's next NAV computation on that business day, which may be at the end of the day or during the day for funds that make multiple NAV computations during a business day. Would this create operational or practical impediments to using the NAV pricing approach? If so, would these impediments occur in specific scenarios (*e.g.*, with particular types of cross-trade counterparties) or for particular types of registered funds, or would the impediments be broader based for registered funds? How would registered funds weigh any such impediments against the efficiencies that the NAV pricing approach may present?
14. How should funds that compute their NAVs less frequently or more frequently than daily price cross trades? Should the funds that compute their NAV less frequently than daily be able to use NAV pricing only on the days that they perform NAV computations, as proposed? Should these funds be allowed to use NAV pricing by following their NAV pricing procedures to price cross trades on days the funds do not compute their NAVs?

Are there any impediments to using the next NAV computation for funds that make more than one NAV computation daily?

15. How should money market funds that use the amortized cost method of valuation under rule 2a-7 implement NAV pricing to price a cross trade? Should these funds be required to use their market-based NAV prices, as proposed, or should they be able to use the amortized cost value of a security for cross trades?
16. Rule 2a-4 under the Investment Company Act permits funds to reflect changes in holdings of portfolio securities in fund NAVs on the next business day. As a result, registered funds currently may not value newly acquired securities on the day of acquisition. How would this affect the use of NAV pricing for cross trades?
17. Under the current market pricing approach, should we permit the registered fund's adviser to determine a price that reasonably represents the current market price using one or more unaffiliated pricing sources, as proposed? Do advisers need additional requirements or guidance on how to make these determinations? Please provide specific information on what requirements or guidance would be helpful and how. For example, are there circumstances when listed equity securities would not be priced using the last reported sale price or, if there are no reported transactions on that day, the average of the highest current independent bid and the lowest current independent offer? If so, what are they, and how would the adviser determine a price?
18. What unaffiliated pricing sources would an investment adviser use to determine the price that reasonably represents the current market price for a security under the proposed methodology? Should the rule or Commission guidance address the use of particular

pricing sources, for example, electronic trading platforms? If so, how? How are unaffiliated pricing sources offering intra-day information (for example, for which asset classes, at what frequency, and using what delivery method)?

19. Should a pricing source be required to be unaffiliated, as proposed? Should we, as proposed, define “unaffiliated” as persons other than first- or second-tier affiliates? Should a fund be permitted to use a pricing source that is affiliated with the registered fund or investment adviser to determine the current market price under certain circumstances (*e.g.*, if the pricing source is widely recognized and used by non-affiliated parties, or if certain information barriers are in place designed to prevent personnel involved in cross-trading decisions from influencing the price provided by the pricing source)? Should a fund be permitted to use quotes from a broker-dealer that is affiliated with the registered fund or investment adviser under certain circumstances? How have registered funds applied the current rule’s provision about effecting cross trades at the “independent current market price”? Would our proposal lead to different results regarding the independence of the cross-trade price?
20. Instead of requiring an unaffiliated pricing source, should we require that pricing sources be subject to oversight so that there is a reasonable basis to use the pricing information as an input for cross trades, similar to the oversight requirement in rule 2a-5? If yes, should the adviser, CCO, board, or some other party be placed in charge of pricing source oversight?
21. As proposed, should we require the adviser to periodically review the reasonableness of prices used under the current market pricing approach? Is the adviser better situated to

conduct this review or should other parties, such as an unaffiliated third-party, the fund's CCO, or board, be involved? Should the rule prevent a fund's portfolio manager or other personnel from being involved in, or responsible for, the periodic review to address potential conflicts? Should the rule specify a frequency for these reviews (*e.g.*, annual, quarterly, monthly)? Separate from the compliance oversight provisions discussed below, should we require that another party, such as an unaffiliated third party, validate the results of the adviser's review?

22. How similar or different should these reasonableness reviews be to the review and testing of funds' fair value methodologies and oversight of pricing service providers conducted under rule 2a-5? Should we more directly link these processes in rule 17a-7 or in Commission guidance?
23. How would the use of the proposed current market pricing approach affect registered funds' valuation processes? Would cross-trade prices using the proposed current market pricing approach help improve valuation processes, and if so, how?
24. If a registered fund and its eligible affiliate cannot agree on a price for the cross trade, the trade will not occur. Are there circumstances in which a registered fund and its eligible affiliate would arrive at different prices for a cross trade they want to engage in under the proposed rule and, if so, what are those circumstances and how likely are they to occur? Relative to the current rule, would the proposed rule increase, decrease, or have no significant effect on the likelihood that a registered fund and its eligible affiliate cannot agree on a price for a cross trade? Are there changes we should make to facilitate agreement on price? For example, if a registered fund and its eligible affiliate ascribe

different values to the same security in a cross trade, should we require or permit use of the average price in these circumstances? Should this be permitted or required only when the parties to a cross trade are both registered funds and/or only when NAV pricing is used? Are we correct in assuming that the differences in value, when they do occur, would be minimal? Should we instead require or permit some other solution, such as using the trade price at the value that the buying or selling registered fund would ascribe to the security?

C. Transaction Fees

We propose to condition the exemption on no consideration, other than cash payment against prompt delivery of a security, and no remuneration being paid in connection with the transaction, other than *de minimis* payments to unaffiliated parties for services provided for clearing, settlement, custody, recording, or reporting of the transaction.⁷⁷ As discussed further below, this condition retains the current rule's focus on limiting costs associated with the transaction to reduce the potential for conflicts and promote the cost-saving benefits of cross trading while permitting the payment of administrative fees where necessary to effect the transaction.

Current rule 17a-7 has similar conditions. One condition in the rule prohibits the payment of consideration other than cash payment against the prompt payment of a security, and another provides that no brokerage commission, fee (except for customary transfer fees), or other remuneration may be paid in connection with the transaction.⁷⁸ The limit on remuneration allows

⁷⁷ See proposed rule 17a-7(b)(3).

⁷⁸ See current rule 17a-7(a) and (d).

cross trades only in those instances where the registered fund would avoid paying traditional transaction expenses, a key purpose of the rule. In response to the Staff Statement, however, some suggested that the current provision lacks clarity regarding what constitutes a customary transfer fee, including, for example, payments related to clearing and settlement, transfer fees to a custodian, or recordation fees to an administrative agent.⁷⁹ To address these issues, some recommended eliminating this condition, allowing registered funds to pay any fee that is appropriate to the services offered.⁸⁰ Others suggested clarifying the scope of fees that are permissible in connection with cross trades.⁸¹

Restrictions on the payments of fees in connection with cross trades continue to be necessary and appropriate. A major benefit of cross trades is lowered transaction costs to registered funds that accrue to the benefit of registered fund shareholders, as many observed in response to the Staff Statement.⁸² A general restriction on remuneration for cross trades provides appropriate safeguards so that registered fund shareholders benefit from lower transaction costs associated with cross trading. We are, however, proposing to modify this condition to modernize the rule and address interpretive questions raised by members of the public.

The proposed condition continues to include a general restriction on the payment of remuneration in connection with the transaction for the reasons discussed above. We also are

⁷⁹ See, e.g., Letter from Invesco Ltd. (Apr. 12, 2021) (“Invesco Letter”); MarketAxess Letter; Letter from Jack W. Murphy (May 6, 2021) (“Murphy Letter”).

⁸⁰ SIFMA AMG Letter; MarketAxess Letter; FIMSAC Recommendations (“the Committee recommends that the SEC make it clear that custodial fees and the fees of electronic trading platforms or dealers can be paid in connection with effecting cross trades involving [registered] funds”).

⁸¹ Invesco Letter; Murphy Letter; ICI Letter.

⁸² See, e.g., ICI Letter; SIFMA AMG Letter; Letter from Pacific Investment Management Company LLC (Apr. 9, 2021) (“PIMCO Letter”).

proposing to amend the rule’s current prohibition on the payment of any fee (except for customary transfer fees) or other remuneration to provide an exception for certain *de minimis* payments to unaffiliated service providers. Permitting only *de minimis* payments to unaffiliated service providers is designed to: (1) limit the potential for conflicts, consistent with the underlying purpose of section 17 and (2) safeguard against transactions being effected for the benefit of other affiliates.⁸³ The language allowing certain payments to unaffiliated service providers would replace the current rule’s language about customary transfer fees.

The proposed condition would permit *de minimis* payments relating to the clearing, settlement, custody, recording, or reporting of cross trades.⁸⁴ Providing a specific list of administrative services for which payment is permitted is designed to provide greater assurance as to which fees are permissible under the rule than the current provision’s exception for “customary” transfer fees. For example, we understand that a custodian, broker-dealer, or trading platform may help settle a cross trade and charge a service or administrative fee for these purposes.⁸⁵ In addition, we understand that in some non-U.S. markets registered funds are required to make certain payments to broker-dealers or trading platforms in order to effect cross

⁸³ The proposed rule would define “unaffiliated” to be a person other than an affiliated person or promoter of, or principal underwriter for, a fund (*e.g.*, a first-tier affiliate) or an affiliated person of such entities (*e.g.*, a second-tier affiliate), consistent with the coverage of section 17(a).

⁸⁴ See ICI Letter; Invesco Letter. Such *de minimis* payments include the equivalent payments on a blockchain or other distributed ledger. For example, gas fees on the Ethereum blockchain are required for processing transactions and are used to maintain and secure the blockchain. We would consider these payments to relate to the clearing, settlement, custody, recording, or reporting of cross trades under the proposal.

⁸⁵ See, *e.g.*, FIMSAC Recommendation (discussing the treatment of custodial fees related to the transfer of a security from one client account to another client account or a fee charged by an electronic trading platform for a dealer to effect a cross trade for an asset manager client under current rule 17a-7).

trades, such as stamp duties, transaction taxes, asset-based transaction fees, custodial fees, settlement fees, or other similar fees.⁸⁶ These payments are customary in the relevant market and are unavoidable when effecting a cross trade in certain jurisdictions. Because these payments relate to the clearing, settlement, custody, recording, or reporting of the cross trade, the proposal would expressly permit these payments despite the general prohibition on payment of remuneration.

A *de minimis* amount for these purposes would depend on the facts and circumstances of the registered fund and the overall context of the fee being paid. In general, the amounts would be small relative to the size of the transaction—and below what a fund would pay in brokerage commissions, bid-ask spreads, mark-ups and mark-downs or otherwise if the fund were to purchase or sell the security in the market. In order to satisfy its obligations under rule 38a-1 to have policies and procedures reasonably designed to prevent violations of the Federal securities laws, a registered fund’s cross-trading policies and procedures should address how the fund will determine whether a given fee is *de minimis* and whether it is being incurred for a permissible purpose.⁸⁷

Also consistent with the current rule, the proposed condition would include a requirement that the transaction involve no consideration, other than cash payment against prompt delivery of a security. This helps to ensure that cross trades are simple, transparent, and not complicated by

⁸⁶ See, e.g., SIFMA AMG Letter (discussing requirements in India and Brazil, where cross trades must cross the market and involve a broker or in Malaysia, where cross trades are subject to a minimum brokerage commission).

⁸⁷ See *infra* section II.E.

non-cash considerations like in-kind exchanges or other forms of payment. It also provides for prompt settlement of cross trades to avoid intervening market risk.

We request comment on all aspects of proposed restrictions on payment of fees in connection with cross trades, including the following items:

25. Do commenters agree that the cross-trading rule should continue to include a condition restricting the types of permissible payments in connection with the transaction? Have there been any changes in market practice or other reasons to change from the rule's current general prohibition on the payment of remuneration in connection with cross trades? Are there circumstances in which remuneration to a broker-dealer, electronic platform provider, or other party beyond the administrative services proposed in the rule would be appropriate? As an alternative, should we omit the proposed condition and explicitly require advisers to include a consideration of remuneration paid in their determination that a transaction is in the best interest of the registered fund? If so, should we describe what factors advisers must or should include in their consideration of remuneration paid? Are there other methods of safeguarding against the potential for payments that are indirect compensation for other services the third party provides?
26. Are there instances when an affiliated party might need to be compensated for administrative services in connection with a cross trade? What conditions would permit appropriate payments while safeguarding against the potential for overreaching or self-dealing? Conversely, should the adviser bear any costs for administrative services provided by affiliated service providers (or should these fees be waived by the service provider) to protect the registered fund from the possibility of overreach or self-dealing?

27. Should we, as proposed, define “unaffiliated” as persons other than first- or second- tier affiliates?
28. Does the proposed provision for “clearing, settlement, custody, recording, or reporting of the transaction” include the full scope of administrative services provided by third party providers that may be necessary to effect a cross trade? Are there any services we need to further clarify? Are there any types of fees that third parties may charge in connection with facilitating a cross trade that the rule should more clearly address? To what extent would advisers anticipate needing to pay for data, such as data from a pricing service, to price a cross trade where the fund is not already obtaining that data to determine the fund’s net asset value or for another purpose? Should we modify the rule to permit this form of remuneration to be paid in connection with a cross trade?
29. In non-U.S. jurisdictions, are there fees that are customary fees in the relevant market and are unavoidable when effecting a cross trade in that jurisdiction but do not relate to the clearing, settlement, custody, recording, or reporting of a cross trade? If so, please describe such fees and whether the rule should more clearly permit these fees.
30. Do commenters agree that the provision, in combination with the proposed oversight and best interest requirements, sufficiently limits excessive payments? Is there any alternative condition we should include to ensure that the amount of payment for administrative services is appropriate? Should the CCO or adviser be required to document the basis for concluding that any administrative fee paid in connection with the transaction is for a necessary administrative service and is *de minimis*?

31. Should we specify what specific amounts should be considered *de minimis* for purposes of this provision or provide a safe harbor amount (*e.g.*, as a percentage of the transaction price)? How would we establish such amount in a way that is flexible enough to not permit excessive payments by all sizes of registered funds? Should this specify that *de minimis* means an amount less than what a fund would pay in transaction costs to purchase or sell the security in the market?
32. Should we make any changes to the current rule’s requirement that cross trades involve no consideration other than cash payment against prompt delivery of the security? Is there any reason to permit in-kind cross trades? If so, what limitations would be needed to prevent overreach or self-dealing?

D. Best Interest Determination and Consistency with Fund Policies and Strategies

The proposed amendments would require a registered fund’s investment adviser to determine prior to the cross trade that the cross trade is in the best interest of *each* registered fund involved in a transaction (which determination, for the sake of clarity, is not dependent on any benefits enjoyed by another fund to the cross trade).⁸⁸ The proposed amendments would also require that a cross trade be consistent with the registered fund’s policies and investment strategies.⁸⁹

⁸⁸ See Federated No-Action Letter; Liquidity Rule Adopting Release, *supra* note 69, at text accompanying n.799 (noting “that cross trading also implicates a fund’s adviser’s duty to seek best execution for each fund or other advisory client, as well as its duty of loyalty to each fund or other advisory client”); proposed rule 17a-7(b)(5). Although the proposed amendments to rule 17a-7 would not require an investment adviser to make a best interest determination as to a non-registered fund client involved in a cross trade, the adviser still owes that client a fiduciary duty and remains subject to the antifraud provisions of the Advisers Act and other Federal securities laws with respect to its advice to that client. See *supra* notes 7-8 and accompanying text.

⁸⁹ See proposed rule 17a-7(b)(4).

The best interest determination requirement is consistent with the adviser's fiduciary duty, or its obligation to act in the best interest of each client. We are proposing to require a best interest determination for each cross trade to help ensure that an investment adviser puts the interests of each fund and its shareholders above its own and does not favor one client over another, and to address the investment adviser's responsibilities as they relate specifically to cross trades.⁹⁰ Cross trades implicate heightened conflicts of interest, which require careful consideration as to whether a particular cross trade is in the best interest of each registered fund involved in the transaction. If an adviser can obtain a more favorable outcome for a fund by trading in the open market (including if more favorable pricing is available in the open market), buying or selling a different security, or not transacting at all, the cross trade is not in the fund's best interest.

Appropriate factors for an adviser to consider when determining if a cross trade is in the fund's best interest could include, for example:

- The investment rationale (*i.e.*, the investment-related justifications) for the cross trade and the expected effect of the cross trade on the fund's performance (*e.g.*, is the cross trade expected to improve, harm, or have no effect on the fund's performance);
- The characteristics of the cross-traded security, including its liquidity;

⁹⁰ See Standard of Conduct Release, *supra* note 7, at n.23 and accompanying text (describing an adviser's fiduciary duty, including the duty of loyalty and duty of care) and n.54 (noting that the duty of loyalty requirement prohibiting an adviser from putting its own interests above its client's also would prohibit the adviser from favoring certain client accounts that pay higher fee rates to the adviser over other client accounts).

- The method of pricing the cross trade, whether more favorable pricing appears to be available in the open market, and any cost savings associated with conducting a cross trade;
- The execution method, quality, and speed, and any associated costs;
- The timing and urgency of the transaction;
- The size of the trade and the expected effect on the price of the security if that volume of securities were purchased or sold on the open market;
- The characteristics of the eligible affiliate, including its expense and fee structure; and
- Current market conditions, especially if the markets are stressed.

The proposed best interest determination is distinct from the other proposed conditions in rule 17a-7(b) and must be considered separately. An adviser could not determine that a cross trade is in the best interest of a registered fund simply because the other conditions of the rule, including the pricing conditions, are met. Although the best interest determination is a separate condition, other conditions of the rule relate to topics that are relevant and may inform the adviser in the best interest determination, such as pricing and transaction fees. For example, with respect to pricing, an adviser should consider how the approach to pricing the cross trade under the rule affects best interest considerations (*e.g.*, if current market pricing is used, the quality of the unaffiliated pricing source(s) used for the transaction). Further, if a trade would be in such volume as to move the market price, conducting the trade as a cross trade may require a heightened level of review of price before the investment adviser determines that it is in the best interest of the fund because such cross-trade price would not incorporate the market moving price effects. As another example, while the proposal would permit the payment of certain *de*

minimis transaction fees in connection with cross trades, an adviser should consider whether paying such fees in a cross trade affects the best interest determination.

While the process and factors for making the best interest determination should be tailored based on the registered fund and the specific circumstances of the cross trade, the proposal would not preclude an adviser from using standardized internal forms in its process that are automatically populated with, or include dropdown menus of, preapproved reasons that the adviser has pre-selected based on its experience and expertise so long as this approach would facilitate accurate documentation of the best interest determination for purposes of the rule's CCO review and recordkeeping requirements. In order to satisfy its obligations under rule 38a-1 to have policies and procedures reasonably designed to prevent violations of the Federal securities laws, a registered fund's cross-trading policies and procedures should address how a registered fund's investment adviser would determine whether a cross trade is in the best interest of the fund, including the process and factors that lead to the determination.⁹¹

The proposal would require the investment adviser to make the best interest determination, but it does not specify particular investment adviser personnel who should make these determinations. In determining which personnel would be appropriate for making the determination, one consideration for an adviser would be the person's role in making the investment or trading decision to cross trade a security. For example, relying upon personnel that have a direct role in making investment decisions for a fund involved in the transaction, such as a portfolio manager, may prove beneficial in that they would have the most direct knowledge of

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See infra section II.E.

the suitability of the trade for a fund. However, while a portfolio manager may have an incentive to obtain positive results for each fund involved, it is also possible that such portfolio manager would have an incentive to favor the performance of one party to a trade over the other because, for example, one party pays higher fees, including performance fees.⁹² In determining which personnel are appropriate for making the best interest determinations, the adviser should carefully consider potential conflicts of interest between potential personnel and each of the funds involved in the transaction. Personnel who provide oversight, monitoring, or review may also be useful in assisting in the best interest determination, but it is possible that they are not best placed solely to make the determination. If the cross trade is between two registered funds, a best interest determination must be made by personnel representing each registered fund. Those personnel might be the same; however, they must make separate determinations, considering the facts and circumstances of each registered fund.

Separate from the best interest requirement, the proposed rule would require that a cross trade be consistent with the registered fund's policies and investment strategies, as recited in its registration statement and reports filed under the Investment Company Act.⁹³ The investment

⁹² The Commission has brought enforcement actions against advisers that allegedly favored one party to a cross trade over another party. *See, e.g.*, Putnam Investment Mgmt., LLC and Zachary Harrison, Investment Company Act Release No. 33257 (Sept. 27, 2018) (portfolio manager prearranged contemporaneous purchases and sales between registered funds in a manner that allegedly favored purchasing funds and disadvantaged selling funds); Macquarie Investment Management Business Trust, Investment Company Act Release No. 35325 (Sept. 19, 2024) (adviser arranged contemporaneous purchases and sales between affiliated selling accounts and registered funds in a manner that allegedly favored the selling accounts and disadvantaged the purchasing funds).

⁹³ Currently, one of the conditions of rule 17a-7 is that “[t]he transaction is consistent with the policy of each registered investment company and separate series of a registered investment company participating in the transaction, as recited in its registration statement and reports filed under the [Investment Company] Act.” The proposal would revise the language to more clearly refer to the registered fund’s investment strategies as well as policies. The current condition, which the Commission included in the original rule adopted in

adviser may determine whether the cross trade is consistent with the registered fund's policies and investment strategies in conjunction with its best interest determination or separately.

We request comments on the proposed best interest determination:

33. Is the proposed best interest determination condition appropriate or necessary?
34. Who should make the best interest determination? Is the investment adviser the appropriate party? If so, are there any concerns of a conflict of interest and could those concerns be mitigated? If not, who should make the determination? Should we provide more detail or guidance on which personnel are best placed to make the best interest determination? If so, which personnel would be most qualified?
35. Should we provide more detail in the rule or guidance on how an adviser should make a best interest determination and what it should consider? For example, should the rule require that an adviser must always consider certain factors in making its best interest determination (*e.g.*, the expected effect of the cross trade on the registered fund's performance; the characteristics of the cross-traded security, including its liquidity; and the cost savings of the cross trade)? Please provide specific information on what detail or guidance would be helpful.
36. Should the rule, as proposed, specifically provide that the investment adviser should make the best interest determination prior to the cross trade? Why or why not? Are there circumstances in which it would be reasonable for an adviser to make a best interest

1966, was designed to address the risk of overreaching in cross trades. See 1966 Adopting Release, *supra* note 4. Including an express reference in the rule to the fund's investment strategies would be consistent with this purpose.

determination after executing a cross trade and, if so, what are those circumstances?

Should we require the best interest determination to be made on a transaction-by-transaction basis or are there circumstances in which an adviser could reasonably make a best interest determination in advance for certain categories of cross trades? If so, how far in advance and for what categories?

37. Should the proposed rule require any particular form of documentation to be maintained under this new condition?

38. Do investment advisers have concerns that it will be difficult to make these determinations? Could this place an undue burden on smaller investment advisers or funds or on specific types of funds, such as internally managed funds? Are there special concerns for advisers and funds with automated or algorithmic trading, because, for example, such trading is generally designed to have minimal human involvement and the best interest determination would require at least some human involvement or because such systems pose the risk that programming problems could cause it to fail to prohibit affiliated trades? Are there instances where the best interest determinations would be automated or done according to an algorithm with no human oversight other than CCO and board review? What benefits and risks would be associated with such an approach, and should this approach be permitted under rule 17a-7?

E. Oversight

We propose to require the registered fund's CCO, instead of its board, to review cross trades, while still requiring oversight by the fund's board. Specifically, the CCO would be responsible for reviewing all cross trades at least quarterly to determine their compliance with

the proposed rule (“quarterly review”) and at least annually to determine if they may have disadvantaged the registered fund relative to the eligible affiliate (“annual review”).⁹⁴ As part of the annual review, the CCO would also review other transactions by the fund or information necessary to evaluate cross trades (including the timing and price of any subsequent sale of a security purchased in a cross trade). The CCO would be required to report the results of these reviews to the registered fund’s board.⁹⁵ These reviews would replace the current rule’s requirement that the board determine at least quarterly that the cross trades were done in compliance with the registered fund’s rule 17a-7 procedures.⁹⁶ The proposal would also eliminate the current requirement that the board adopt, and make and approve changes to, the cross-trade procedures.⁹⁷ The proposed amendments are designed to better align oversight requirements to business responsibilities, reduce the burden on boards associated with rule 17a-7, and remove duplication with rule 38a-1.

1. Responsible Parties

Currently, the rule requires that the board adopt, and make and approve changes to, the fund’s cross-trade procedures, and review cross trades quarterly. The proposal would remove the quarterly review requirement from the board’s responsibilities and place it on the CCO, who is already responsible for administering the registered fund’s compliance policies and procedures, including those pertaining to cross trades, while maintaining board oversight through reports of

⁹⁴ See proposed rule 17a-7(b)(7)(i) and (ii).

⁹⁵ See proposed rule 17a-7(b)(7)(iii).

⁹⁶ See current rule 17a-7(e)(3).

⁹⁷ See current rule 17a-7(e)(1)-(2).

the CCO's review of cross trades.⁹⁸ Accordingly, the proposed rule would provide layers of protection for investors against conflicts of interest implicated by cross trading and better align oversight requirements to business responsibilities.

Under the proposal, the CCO would be responsible for reviewing cross trades at least quarterly to determine whether they are compliant with the rule and at least annually to determine whether a cross trade or set of cross trades may have disadvantaged a registered fund relative to its eligible affiliate. Finally, the board would receive quarterly and annual reports from the CCO on the results of the quarterly review and annual review, respectively.⁹⁹ This requirement is designed to facilitate the board's oversight of the fund's cross-trading activities and would remove the need for the board to determine quarterly that cross trades were made in compliance with the procedures as is required under the current rule.¹⁰⁰ The proposed amendments would allow boards to focus on larger issues, including conflict of interest concerns, arising out of the CCO's reports, rather than a more granular focus on whether each cross trade complied with the fund's cross-trading policies and procedures as currently required under rule 17a-7. Although the proposed amendments would modify the oversight framework, boards should continue to engage actively in overseeing and asking questions about cross-trading activity, particularly given the conflict of interest considerations it raises. By better aligning the responsibilities of oversight to the business responsibilities of the CCO and the board, the

⁹⁸ See rule 38a-1(a)(4).

⁹⁹ Consistent with the current rule, the proposed rule would require that the registered fund's board of directors satisfy the fund governance standards defined in rule 0-1(a)(7). See proposed rule 17a-7(b)(6).

¹⁰⁰ See current rule 17a-7(e)(3).

proposal is designed to increase efficiencies while providing multiple layers of protection for investors.

2. Quarterly and Annual Reviews and Reports

Currently, the board must determine no less frequently than quarterly that all cross trades made during the preceding quarter were effected in compliance with the cross-trade procedures.¹⁰¹ The proposal would remove this requirement and replace it with the requirement of the CCO's quarterly and annual reviews and reports to the board, which would provide the CCO and board multiple opportunities for review or oversight of cross trades. At a minimum, quarterly reviews would comprise of a technical compliance check of whether individual trades met the conditions of the rule, similar to the current rule's requirement that the board determine quarterly that cross trades complied with the fund's procedures. In comparison, annual reviews would be an opportunity for the CCO to perform a holistic review over a longer period to determine whether the registered fund was disadvantaged, for example, by identifying indicators of parking, dumping, or cherry-picking. The annual and quarterly reviews and reports are designed to work together, providing snapshots of a fund's cross-trading activity at different points in time, providing the CCO and board with the information necessary to monitor and oversee the investment adviser's cross-trading activities, identify any problems, and help limit overreaching.

Quarterly reviews by the CCO would help provide opportunities to monitor the procedures, identify any aspects of the procedures that are not working as intended and that need

¹⁰¹ See *id.*

adjustment, and detect any cross trades that did not comply with the proposed rule. A quarterly review would encompass all cross trades effected during the period and would be required to include information to determine whether trades complied with the conditions under the proposed rule, such as whether:

- Each cross trade occurred with an eligible affiliate;
- Each security was eligible to be cross traded;
- The price was determined in compliance with the rule;
- Any fees paid in connection with a cross trade were consistent with the rule;
- Each cross trade was consistent with the registered fund's policies and investment strategies; and
- The investment adviser determined that each cross trade was in the best interest of the registered fund.

The quarterly review cadence would be consistent with the current rule's requirement for the board to determine compliance with the cross-trade procedures. The proposal would require the CCO to provide a quarterly report to the board on the results of the quarterly review. These quarterly reports would facilitate the board's oversight by providing timely information about the fund's cross trades and the efficacy of the fund's cross-trading policies and procedures.

The proposed amendments also would require that the CCO review annually cross trades as well as other transactions or information necessary to evaluate the cross trades to help the CCO determine if the cross trade, or a pattern of cross trades, may have disadvantaged the registered fund relative to the eligible affiliate. As part of the annual review, the CCO would be required to review the timing and price of subsequent sales by the registered fund of securities it

purchased in a cross trade. This requirement is designed so that the CCO reviews not only a cross trade itself, but also any other transactions or information necessary, to analyze whether the fund may have been disadvantaged by the cross trade or by the cross-trading arrangements more broadly. The CCO may conduct the annual review in a variety of ways, including, for example, by testing a sample of cross trades, automated monitoring and scanning of cross trades, or forensic testing to better identify patterns and trends that may show a fund being disadvantaged by a cross trade.

The annual review would cover more cross trades over a longer period, which would provide better information to the CCO, especially in identifying a pattern of transactions that may disadvantage a fund relative to the eligible affiliate. For example, an analysis of larger or longer datasets may help identify a pattern of favoring an eligible affiliate that charges a higher management fee such as a performance-based fee. These or other patterns may be more difficult for the CCO to detect when reviewing, on an idiosyncratic basis, at or near the time of the cross trade. An annual review is designed to balance the time that might be needed to detect these patterns with the disadvantages that the fund and its shareholders may suffer. The reviews also have different, but complementary, primary focuses: the quarterly review would focus on whether each cross trade effected during the quarter complied with the rule's conditions, while the annual review would utilize data across the entire life cycle of a given investment holding to more holistically assess whether the fund was disadvantaged by any given cross trade or pattern of cross trades.

The proposal would specifically require that the CCO, as part of the annual review, review the timing and price of subsequent sales of securities purchased in cross trades (a

“disposition price”) to determine if the fund was disadvantaged by cross trades. The CCO may conduct this review using any testing method, including sampling a selection of cross trades to analyze and compare their disposition price to the cross-trade price. While funds would be required to conduct this analysis regardless of the timing of the disposition, this type of testing may be particularly helpful when the cross-traded security is disposed of close-in-time to the cross trade as many considerations may factor into a disposition price.

The proposed rule would also require the retention of the information or materials upon which the CCO’s determinations are made, which would include information or materials related to other transactions or information reviewed as part of this annual review.¹⁰² These records are designed so that a CCO would have the necessary information to review the disposition price of any security as compared to the price of the cross trade to identify a pattern of cross trades that may disadvantage a fund. The CCO would not need to review any such cross trades before the adoption of the proposed amendments for subsequent sales.

In connection with the annual review, the CCO generally should also consider other appropriate factors as relevant, including for example:

- The appropriateness of cross-trade prices;
- The performance of cross-traded securities;
- The cost savings of cross trades;
- The volume, frequency, and timing of cross trades;
- The characteristics of the cross-traded securities, including the liquidity profile;

¹⁰² See proposed rule 17a-7(c)(3); see also *infra* section II.G (discussing the proposed recordkeeping requirements).

- The characteristics of eligible affiliates, including their expense and fee structure;
- The quality of unaffiliated pricing sources;
- The execution quality of the cross trade; and
- The market conditions at the time the trades occurred, especially if the markets were stressed.

The CCO may evaluate these factors using any appropriate testing method. For example, to determine whether the cross-trade price is appropriate, the CCO may review the investment adviser's determination or process for determining that the cross-trade price reasonably represented the current market price for the security using unaffiliated pricing sources. The CCO may also back test or validate the price, as appropriate, against: (1) NAV pricing, if the cross-trade price is determined using current market pricing, (2) pre-trade quotes or prices, or (3) other observed transactions or market information. If the investment adviser's approach to determining cross-trade prices consistently over- or under-prices securities as compared to observed market transactions or valuations used for NAV purposes, the CCO should investigate the reason for the difference and consider whether use of that approach for pricing cross trades continues to be reasonable. Other testing methods include, for example: comparing the performance of the cross-traded securities against the fund as a whole; comparing the estimated cost savings of a cross trade against the costs of a similar arms-length transaction; monitoring relative volume and frequency of cross trades for a fund against previous periods; determining if the cross trades are consistent with the fund's investment policies and strategies; examining the characteristics of the cross-traded securities, such as if they are newly issued or their availability in the market; analyzing execution of the cross trade, including speed, market impact, execution quality; and

monitoring the timing of a cross trade, for example, if a cross trade is done in stressed market conditions. These types of testing can often reveal important information about the continuing appropriateness of the registered fund's cross-trade policies or practices. Testing methodologies may develop, improve, and change over time. We would expect the CCO to be empowered to ask for any appropriate information in the course of the quarterly or annual reviews and reports.¹⁰³

A cross-trade review may also be combined with other compliance reviews. The cross trade annual review may be completed simultaneously with the annual review required by rule 38a-1 of the adequacy of the policies and procedures of the fund and the effectiveness of their implementation. Combining reviews may increase efficiencies and improve the quality of the review by allowing the CCO a more comprehensive view of the fund's policies and procedures, including those involving cross trades. As another example, a fund may experience cost savings and efficiencies if it combines its review and due diligence of the same vendor that is used both as an unaffiliated pricing source under rule 17a-7 and as a pricing service provider under rule 2a-5.

The timing and format of the CCO's quarterly and annual reports would depend on the facts and circumstances. The CCO and board may determine that summaries are sufficient for the reports.¹⁰⁴ While reviews and reports are required quarterly and annually, they could be

¹⁰³ See also Compliance Programs of Investment Companies and Investment Advisers, Advisers Act Release No. 2204 (Dec. 17, 2003) [68 FR 74714 (Dec. 24, 2003)] ("Compliance Programs Release"), at n.75 and accompanying paragraph.

¹⁰⁴ This is similar to how directors may satisfy their obligations under rule 38a-1 by reviewing summaries of compliance programs. See *id.*, at text accompanying n.33.

performed on an as needed or more frequent basis as well. For example, a registered fund that has higher volumes of cross-trading activities may warrant more frequent review. Fund or investment adviser personnel other than the CCO may contribute to the report, as cross trades may touch multiple business functions, including portfolio management and trading. The information or materials considered as part of the CCO's reviews and the reports to the board are required to be documented, and should be documented in a manner that best suits the fund's cross-trading policies and internal practices.¹⁰⁵ The CCO's annual review and report to the board may include an analysis of such matters as: whether the cross-trading policies and procedures are working as intended; whether the content, structure, and timing of the review and report are appropriate; and whether any changes are needed to the fund's cross-trading policies and procedures. The annual report may also include a discussion of any actions taken if a cross trade is found to disadvantage a fund. As with other policies and procedures, the board would be able to request and review any other related materials.¹⁰⁶

3. Policies and Procedures

Currently under rule 38a-1, the board is responsible for approving registered fund written compliance policies and procedures, reviewing their adequacy and effectiveness of implementation, and determining that they are reasonably designed to prevent violation of the

¹⁰⁵ See proposed rule 17a-7(c)(2) through (4); see also *infra* section II.G (discussing the proposed recordkeeping requirements).

¹⁰⁶ See, e.g., Compliance Programs Release, *supra* note 103, at n.65 and accompanying text (stating, for example, that the fund's governance related policies and procedures should be designed to guard against the failure of the board to request and consider information required by the Investment Company Act from the adviser and other service providers).

Federal securities laws.¹⁰⁷ In many respects, this is duplicative of the current requirement under rule 17a-7 for the board to adopt, make, and approve changes to the registered fund's cross-trade procedures, and we propose to remove this requirement from rule 17a-7.¹⁰⁸ Instead, the board would approve policies and procedures under rule 38a-1 that are reasonably designed to prevent violations of section 17(a) by, among other things, conducting cross trades that would comply with proposed rule 17a-7. At a minimum, the policies and procedures should address how the fund and adviser will effect cross trades to satisfy the conditions of the proposed rule. The policies and procedures generally should describe how the CCO would conduct the quarterly review to determine compliance with the requirements of the proposed rule, for example, by examining any portfolio manager input in determining whether a security is eligible for cross trading, reviewing the adviser's best interest determination for any irregularities, and confirming that the cross trade is consistent with the fund's other policies and investment strategies as stated in its registration statement. They generally should also describe how the CCO would conduct the annual review, for example, by describing the review of other transactions or information, the disposition price, any relevant factors, and any appropriate testing to determine that a cross trade did not disadvantage a fund.

Rule 38a-1 provides flexibility for funds and fund complexes to apply the requirements of the rule in a manner that best suits the organization.¹⁰⁹ In the case of cross trades, the board

¹⁰⁷ See rule 38a-1(a)(1) - (3).

¹⁰⁸ See current rule 17a-7(e)(1) and (2).

¹⁰⁹ See Compliance Programs Release, *supra* note 103, at n.30 and accompanying paragraph.

could consider the fund's circumstances and use of cross trades, which may include considerations such as the registered fund's investment objective and strategies, risk and liquidity profile, conflicts of interest with eligible affiliates, potential cost savings, and market conditions. The policies and procedures should be tailored to each registered fund.¹¹⁰ For example, a registered fund that only occasionally cross trades exchange-traded equity securities using NAV pricing may not require the same level of CCO review or detailed reporting to the board as a registered fund that frequently cross trades fixed-income securities using current market pricing.

The registered fund's policies and procedures may set appropriate levels of deviation (*e.g.*, tolerance levels) to trigger further review. For example, registered funds may set a tolerance level for differences between the cross-trade price and the valuation price, which may automatically trigger additional review. As another example, the policies and procedures may set a minimum holding period for cross-traded securities, which may trigger additional review to address any parking or dumping concerns.

The policies and procedures may describe specific circumstances and conditions that bar a cross trade from occurring, prevent them through pre-trade compliance blocks, require additional investigation, or give a CCO or investment adviser personnel complete discretion to prevent a cross trade. For example, pre-trade compliance testing could be implemented for cross trades to determine if they are consistent with a registered fund's investment policies and procedures or other compliance requirements, and trade blocks could be implemented for those

¹¹⁰ However, a board could approve a combined cross-trade policy for multiple registered funds as long as the combined policy meets the requirements under rule 38a-1 and proposed rule 17a-7 for each fund.

that are not. The policies and procedures may also describe any actions that should be taken if a cross trade is found to disadvantage a registered fund relative to an eligible affiliate. Actions might include, for example, depending on all the facts and circumstances, including applicable law, reversing a trade or the adviser making the disadvantaged registered fund whole, together with additional monitoring in the future.

We request comments on the proposed oversight requirements:

39. Are the proposed oversight requirements appropriate? What are the advantages and disadvantages of the proposed oversight requirements?
40. Are the quarterly and annual review and reporting cadences appropriate? Should we instead require only an annual review, similar to that required under rule 38a-1, or conversely only a quarterly review as in current rule 17a-7? Should we provide more detail or guidance on how the quarterly or annual review should be performed and documented? Please provide specific information on what detail or guidance would be helpful.
41. Is the fund's CCO the appropriate party to perform the review and report to the board? Should a fund's investment adviser instead be able to designate the person(s) responsible for reviewing cross-trading activity and reporting to the board, provided the fund's board, including a majority of disinterested directors, approves such designation? What qualifications or limitations should there be on who those persons may be (*e.g.*, only an officer or officers of the fund's investment adviser, or limitations on the ability of portfolio managers to serve in this role)? Should we provide more guidance on which

additional parties may perform or contribute to the review and report to the board? Please provide specific information on what guidance would be helpful.

42. Is the annual requirement to review whether a cross trade or pattern of transactions may have disadvantaged the registered fund relative to the eligible affiliate appropriate? Are there patterns of transactions that may be more difficult or impossible to identify during a quarterly review?
43. Should we provide more guidance on what the cross-trade policies and procedures should include or consider? Please provide specific information on what should be included or considered, and why.
44. Should we provide more guidance on how a CCO should conduct the review quarterly and annually? Should the guidance include other factors and considerations? Please provide specific information on what factors and considerations should be included and why. Should those factors and considerations be specifically listed in the rule? Should we provide more detail or guidance on when the quarterly or annual review should end, for example, one year after the fund's most recent cross trade?
45. What are the advantages and disadvantages of requiring the CCO to conduct disposition analysis by reviewing other transactions or information necessary to evaluate transactions effected under this section (including the timing and price of subsequent sales of securities purchased in cross trades), in determining whether a cross trade may have disadvantaged the fund relative to the eligible affiliate? Should the rule require information other than the timing and price of subsequent sales for the CCO to compare against the cross trade, such as reasons that the disposition price is different from the

cross trade purchase price? Should CCOs be required to conduct similar analyses when a fund sells a security in a cross trade, by considering the timing and price of that cross trade sale relative to the earlier purchase of the security by the fund? Would that type of analysis present additional challenges, such as identifying the time and price of the earlier purchase of the security when the fund has engaged in multiple purchases to build its position in the security over time?

46. Is the proposed role of the board appropriate? Should the rule prescribe the content and format of the reports to the board and how the board should review those reports?
47. Should the oversight requirements instead be proportionate based on the size or characteristics of a registered fund or its cross-trading activity? For example, should certain types of funds be required to have fewer or less frequent reviews and reports to the board (*e.g.*, only annual reviews/reports)? If so, why and for what types of funds (*e.g.*, small funds, funds that engage in a small amount of cross trading relative to their net assets, funds that only cross trade securities that have readily available market quotations, or funds that exclusively use NAV pricing of cross trades)?
48. Should the rule require certain actions if a CCO finds material noncompliance with the proposed rule or a fund's policies and procedures? If so, what should the actions include?

F. Reporting

The proposed amendments would establish new reporting requirements for certain registered funds.¹¹¹ We propose to amend Form N-PORT and Form N-MFP (together, the “forms”) to require certain registered funds to provide additional information about their cross trade-related purchase and sale activity. Specifically, we propose to amend the forms to require registered funds that engaged in cross trades of portfolio investments in reliance on rule 17a-7 during the preceding twelve-month period to disclose, for each asset type (or category of investment, in the case of Form N-MFP) during the reporting period and in U.S. dollars:¹¹²

- The aggregate value of portfolio investments the registered fund purchased under rule 17a-7;¹¹³
- The aggregate value of portfolio investments the registered fund purchased;

¹¹¹ Form N-PORT is used by registered management investment companies, and exchange-traded funds organized as unit investment trusts (“UITs”) but is not used by money market funds or by small business investment companies (“SBICs”) registered on Form N-5. Form N-MFP is used by money market funds.

¹¹² For Form N-PORT filers, asset types are defined as short-term investment vehicle (*e.g.*, money market fund, liquidity pool, or other cash management vehicle), repurchase agreement, equity-common, equity-preferred, debt, derivative-commodity, derivative-credit, derivative-equity, derivative-foreign exchange, derivative-interest rate, derivatives-other, structured note, loan, ABS-mortgage backed security, ABS-asset backed commercial paper, ABS-collateralized bond/debt obligation, ABS-other, commodity, real estate, and other. If other, the registered fund must provide a short description. See Item C.4.a. of Form N-PORT. For Form N-MFP filers, categories of investments include: U.S. treasury debt; U.S. Government agency debt; non-U.S. sovereign, sub-sovereign and supra-national debt; certificate of deposit; non-negotiable time deposit; variable rate demand note; other municipal security; asset backed commercial paper; other asset backed securities; U.S. treasury repurchase agreement; U.S. Government agency repurchase agreement; other repurchase agreement; insurance company funding agreement; investment company; financial company commercial paper; non-financial company commercial paper; tender option bond; and other instrument. If other instrument, the registered fund must provide a brief description. See Item C.6. of Form N-MFP.

¹¹³ While the proposed amendments to Form N-MFP use the term “portfolio securities” rather than “portfolio investments,” reflecting that money market funds invest in a more limited universe of instruments than other registered funds subject to Form N-PORT, we use the term “portfolio investments” throughout this discussion for simplicity.

- The aggregate value of portfolio investments the registered fund sold under rule 17a-7; and
- The aggregate value of portfolio investments the registered fund sold.¹¹⁴

The aggregate value would mean the value of portfolio investments purchased or sold, calculated on a gross basis, without netting any purchases and sales. When providing the aggregate value of portfolio investments purchased or sold under the items mentioned in the second and fourth bullets above, a registered fund should include all purchase or sale transactions, including any amounts purchased or sold in cross trades. The trading information would be reported for the preceding month.¹¹⁵ This disclosure would follow the filing timelines, publication frequency, and reporting period of each form.¹¹⁶

¹¹⁴ See Item B.12 of proposed Form N-PORT; Item A.23 of proposed Form N-MFP.

¹¹⁵ For example, a report providing a registered fund's portfolio holdings as of the last business day, or last calendar day, of the month of April would be required to include information about aggregate trading activity and cross trades the fund effected in the month of April.

¹¹⁶ Currently, Form N-PORT reports for each month in a registered fund's fiscal quarter are filed with the Commission within 60 days of the end of the fiscal quarter, and the report for the third month of the quarter is made public upon filing. In 2024, the Commission adopted amendments to Form N-PORT that require registered funds to file monthly reports within 30 days of month end and that provide for publication of monthly reports with additional delay. These requirements have not gone into effect. See Form N-PORT and Form N-CEN Reporting; Guidance on Open-End Fund Liquidity Risk Management Programs; Delay of Effective and Compliance Dates, Investment Company Act Release No. 35538 (Apr. 16, 2025) [90 FR 16812 (Apr. 22, 2025)]. In 2026, the Commission proposed changes that, among other things, would provide registered funds with additional time to file monthly Form N-PORT reports and restore a quarterly publication frequency. See Form N-PORT Reporting, Investment Company Act Release No. 35962 (Feb. 18, 2026) [91 FR 8582 (Feb. 23, 2026)] ("Form N-PORT Reporting Release"). As the proposed cross-trading reporting requirements would follow the same timeframes as generally required for Form N-PORT, if we were to adopt the Form N-PORT proposal, we also expect that the proposed cross-trading reporting items would be reported and made public at the amended timeframes. If the 2026 amendments in the Form N-PORT Reporting Release are adopted as proposed and the Commission adopts the proposed amendments to rule 17a-7, we would anticipate requiring cross-trade information for each of the preceding three months in each Form N-PORT report to provide transparency in cross-trade information to investors. This would also mitigate concerns that investors might potentially believe that one month's cross trades represent the full quarter and better conform with other information that would be presented on Form N-PORT if the

Currently, most registered funds report on Form N-CEN whether they relied on certain statutory and rule-based exemptions, including rule 17a-7.¹¹⁷ While this information helps identify whether a registered fund made cross trades in the reporting period, it does not provide any additional information, such as the volume of cross trades by registered fund or asset class. Registered funds currently also are subject to requirements to disclose material information about cross trades in their financial statements.¹¹⁸ This information is often in narrative form, which limits comparability, and may not provide a clear picture of the frequency, type, or amount of all cross trades by the registered fund or those that are not deemed material. As suggested by some respondents, reporting aggregated cross-trade information on Form N-PORT could provide additional transparency and visibility into registered funds' cross-trading practices.¹¹⁹ The proposed reporting on the forms would provide information about the total and comparative volume of cross trades by asset class in a structured format that can be efficiently analyzed by the Commission staff and market participants across registered funds in a way that is not currently available through reports on Form N-CEN or in registered fund financial statements.

Similarly, registered funds do not currently disclose the volume of trading activity that occurred during the reporting period, specifically, the aggregate value of portfolio investments that were purchased or sold. Registered funds are currently required to report information on the

2026 amendments are adopted as proposed. Form N-MFP reports are filed on a monthly basis no later than the fifth business day of the month.

¹¹⁷ See Item C.7 of Form N-CEN (requiring this reporting by management investment companies).

¹¹⁸ See 17 CFR 210.6-07 (requiring disclosure of certain affiliated transactions as part of a registered fund's statement of operations) and ASC 850 (requiring disclosure of material related party transaction).

¹¹⁹ See ICI Letter; Capital Group Letter.

forms generally on an “as-of” basis, which provides information at a single point in time, but does not provide this specific information about the volume of investments the registered fund purchased or sold during the period.¹²⁰

This reporting requirement would enable the Commission and its staff and market participants to understand the proportion of a registered fund’s overall trading activity that consists of cross trades, both in the aggregate and within specific asset classes, which would provide necessary context for understanding the volume, significance, and materiality of cross trades relative to total trading activity as well as trends in such activity over time. To provide better contextual information about how the volume of a registered fund’s cross trades compares to its overall trading activity, the proposed reporting requirement would begin when a registered fund begins cross trading and apply for a 12-month period following any cross trades. During this period, the registered fund would be required to report information about its aggregate trading activity by asset class, even if it does not conduct cross trades for particular months within that period. This approach is designed to recognize that the volume and character of funds’ trading activities can vary from month-to-month and also provide an appropriately lengthy period for data review. For example, if we were to instead require aggregate trading information only for months in which a fund conducts cross trades, the aggregate trading

¹²⁰ See, e.g., Item B.7 on Form N-MFP (requiring shareholder flow information as of the close of business on each business day of the month reported).

information for those months may not accurately reflect how the volume of a fund's cross-trading activity compares to its overall trading activities.¹²¹

Since the volume of cross trades can reasonably be expected to grow under the proposed amendments, the proposed reporting requirement would assist in understanding and monitoring the effects of that growth and how it affects specific registered funds and asset classes. This reporting requirement would enhance transparency and facilitate more informed decision-making by providing information on cross-trading activity over time for a registered fund and across similar registered funds by asset class and reporting period.

The proposed reporting is also important because cross trades occur outside of the public markets and do not generate publicly observable market data, unlike transactions on registered exchanges or reported through post-trade transparency systems such as TRACE or RTRS. The lack of public information about specific transaction prices may negatively impact price discovery processes. In addition, the lack of public information about the volume of cross trades may distort perceptions of liquidity in a particular asset class or market. While the proposal would not provide the type of transparency available through systems like TRACE or RTRS, the proposed reporting on the forms would provide volume transparency by requiring reporting of the aggregate volume of cross trades, by asset class. If the volumes of cross trades are growing or substantial, this information may help market participants understand the potential effects of the

¹²¹ Specifically, if we required aggregate trading information only for months in which a fund cross trades, the reported information may over- or under-estimate the proportion of a fund's trading activity that consists of cross trades. For example, if a registered fund engaged in relatively low volumes of non-cross-trading activity in months in which the fund cross traded, but higher volumes of non-cross-trading activity in other months, or only reported for a shorter period than twelve months, the reported information would suggest that cross trading represents a greater volume of the fund's trading activity than it actually does.

cross trades on the reliability of other available information about trading in that asset class. In addition, the proposed reporting may inform any future Commission action about cross-trading data and whether it should be made available through post-trade transparency systems.

As with other information on the forms, the proposed disclosure would be filed in a structured data format. Standardized disclosure on a registered fund's cross trading and total trading activity would provide transparent, standardized, and comparable information regarding the extent to which the registered fund industry, and each individual registered fund, engages in cross trading, overall volumes, as well as the types of assets involved in such trading activities. This allows investors and other market participants to easily access and process the cross-trade information reported, either by analyzing the forms directly or through analyses prepared by third-party service providers, which may enable more informed investment decisions and promote greater accountability by the adviser. This reporting would also provide market participants with information to evaluate the potential effects of cross trades on perceptions of liquidity in a particular asset class or market.

The information we propose to be reported is designed to balance the burden of providing it with the Commission's and the public's need for the information. The proposal would only require registered funds that engaged in cross trades of portfolio investments in reliance on rule 17a-7 during the preceding twelve-month period to provide information about the aggregate value of cross trade-related purchases and sales grouped by asset type or category of investments. While more granular reporting, such as the price and volume of each trade or cross trade, or industry-wide reporting on total trading volumes, would provide valuable information, registered funds would then bear a more significant reporting burden. In addition, the proposed

amendments work with existing recordkeeping obligations under the Investment Company Act, such as the requirement to maintain records of registered funds' portfolio transactions.¹²² The proposed reporting may help mitigate the potential conflicts of cross trading by providing insight into such trading to the Commission and its staff, assisting them in carrying out their regulatory responsibilities, including any future Commission action as to cross trading, risk monitoring during periods of market stress, and regulatory oversight.

We request comments on the proposed reporting requirements:

49. Is the proposed reporting requirement appropriate? For example, is the information that registered funds currently provide on the forms, Form N-CEN, and in financial statements sufficient for the Commission, investors, and other market participants to monitor fund trading activity, including cross trades? What are the advantages and disadvantages of the proposed reporting requirements? If the proposed requirements to Form N-PORT and Form N-MFP are adopted, should we eliminate Item C.7.e. on Form N-CEN, which asks if a fund relied on the rule 17a-7 exemption?
50. Is the proposed reporting trigger for registered funds that engaged in cross trades during the preceding twelve-month period appropriate? Would this approach affect registered funds' ability to automate their filing processes or introduce complexity to the reporting process? For funds that engage in cross trading, how frequently do cross trades occur? Does the frequency at which funds engage in cross trading suggest that it would be unnecessary or ineffective to require reporting over a twelve-month period since the

¹²² See 17 CFR 270.31a-1(b)(1) (requiring, for example, itemized daily records in detail of all purchases and sales of securities).

fund's last cross trade? Should this reporting requirement apply to registered funds that have engaged in cross trades within a shorter or longer period than the preceding twelve months (for example, the past 3, 6, 18, or 24 months)? Should the reporting be limited to only those months in which a registered fund engaged in a cross trade?

51. Instead of using a reporting trigger based on when the fund last engaged in a cross trade as proposed, should we require registered funds to report cross trade and total trading information if a fund has policies and procedures that permit it to cross trade regardless of whether the fund has cross traded? Should the reporting apply to any registered fund that has cross traded or intends to cross trade over a specified period (for example, 1, 3, 6, 12, 18, or 24 months)? Are there other, more effective ways to identify funds that engage in cross-trading activity for purposes of determining which funds must report cross trade-related information?
52. Is the proposed reporting period of the preceding month appropriate? If the 2026 amendments in the Form N-PORT Reporting Release are adopted as proposed, should a registered fund reporting on Form N-PORT be required to disclose for a longer period (for example, each of the preceding three months with the report for the third month of the quarter being made public) to provide for public transparency of the monthly data?¹²³
53. Is the proposed requirement to report the aggregate value of cross trading and all trading activity by asset class or category of investment appropriate? Should the proposed amendments use the investment groupings already established in each form for this

¹²³

See supra note 116.

purpose or should they be modified to better capture trading activity information? If yes, how? Should registered funds instead, or in addition, report trading activity using other measurements, for example, by level within the fair value hierarchy under U.S. GAAP?

54. Is the proposed requirement to report the aggregate value of portfolio investments purchased and sold appropriate? Should registered funds instead, or in addition, report the proportion of total purchases and sales attributable to cross trades? Should registered funds instead, or in addition, report portfolio investments that are acquired or disposed of, or held to maturity? Should reporting of aggregate trading activity be required only for the asset classes in which the registered fund has conducted a cross trade during the preceding twelve-month period, or should reporting of aggregate trading activity be required for all asset classes in the relevant form? Are there certain asset classes in which registered funds are unlikely to conduct cross trades, either due to the conditions of the rule or other considerations, and therefore registered funds should not be required to report aggregate trading activity for those asset classes?
55. Is the term “aggregate value” clear and operationally workable? If not, what additional guidance on specific portfolio investments or how values should be reported would be helpful?
56. Is the proposed requirement to report cross trade purchases and sales transactions separately appropriate? Should registered funds instead, or in addition, report additional information about their aggregate cross-trading activities, for example, the number of cross trades effected during the reporting period or total net realized gains or losses associated with cross-trading activities (or net change in unrealized appreciation or

depreciation)? Should registered funds instead, or in addition, report additional information about individual cross trades, for example, details on the timing, price, and volume of each cross trade, the potential cost savings, and cross-trade parties? If yes, what other information should be disclosed?

57. Should registered funds be required, instead of the proposed reporting requirements or in addition, to publicly report cross-trading activity, for example, through a reporting venue administered by a self-regulatory organization or securities information processor? If yes, why and what method should be used (*e.g.*, reporting individual cross trades to reporting venues such as TRACE and RTRS)? Would this type of public reporting of cross-trading activity assist price discovery and impose pricing discipline? If yes, how? Is some cross-trading activity already being reported, for example by an affiliated broker-dealer? If yes, under what circumstances and how often?

58. Should registered funds instead report the proposed information about trading activity, including cross trades, confidentially to the Commission? If so, why would public disclosure of information about registered funds' trading activities be neither necessary nor appropriate in the public interest or for the protection of investors?¹²⁴

59. Are there any barriers to registered funds reporting trading activity, including cross trades, on the forms? If yes, what are they (*e.g.*, needing to manually process information or link separate information systems)? Would those barriers cause some registered funds

¹²⁴

See section 45 of the Investment Company Act (providing that information filed with the Commission shall be made available to the public, unless the Commission finds that public disclosure is neither necessary nor appropriate in the public interest or for the protection of investors).

to avoid cross trading when cross trading would otherwise be beneficial to the funds? If so, which funds and why? Should there be a *de minimis* exception to reporting (e.g., cross trades that do not exceed 1%, 5%, or 10% of net assets) or should certain funds (e.g., small funds or funds that engage in cross trading only for level 1 securities) be exempt from the proposed reporting requirements?¹²⁵ If so, why and for what types or size of funds or what amount of cross trading? Are there other changes we should make to reduce reporting burdens, such as requiring the proposed information about cross-trading activity but not requiring the proposed information about aggregate trading activity?

60. Some types of funds that may rely on rule 17a-7, such as BDCs and SBICs, are not required to report on Form N-PORT or Form N-MFP and therefore would not be subject to the proposed reporting requirement. Is the information that BDCs or SBICs currently provide on other forms or periodic reports sufficient for the Commission, investors, and other market participants to monitor fund cross-trading activity? Should we amend other reporting forms to require cross-trading information for funds that do not report on Form N-PORT or Form N-MFP? If so, where should this disclosure be located (e.g., in Form 10-K or other periodic reports for BDCs)?

61. Part D of Form N-MFP separately requires all prime money market funds to disclose the gross market value of portfolio securities they sold during the reporting period by category of investment. For prime money market funds that engage in cross trading, the proposal would require the same information under a different item on Form N-MFP for

¹²⁵

See infra note 134 (discussing a pending proposal addressing the definition under the Investment Company Act of small organization and small business for purposes of the Regulatory Flexibility Act).

a 12-month period after any cross trade (in addition to the aggregate value of portfolio securities purchased or sold in cross trades, and the aggregate value of portfolio securities purchased). Recognizing that the proposed reporting requirement and Part D of Form N-MFP differ in the scope of money market funds subject to the reporting requirements, are there ways in which we should consolidate the reporting requirements for prime funds that engage in cross trading? Would such consolidation reduce reporting burdens without affecting the utility of the reported information?

G. Recordkeeping

We propose to update the recordkeeping requirements of rule 17a-7 to reflect the proposed amendments. The current recordkeeping requirements under the rule and proposed changes are set forth in Table 1 below.

Table 1

Record	Current Rule	Proposal
Written Policies and Procedures	Rule 17a-7(g)(1): Maintain and preserve permanently.	Removed.
	Rule 38a-1: Maintain all policies and procedures that are in effect or were in effect at any time during the last five years.	No change.
Transaction Records (including description of security, identity of counterparty, and terms of the transaction)	Six years from the end of the fiscal year in which a rule 17a-7 transaction occurred, the first two years in an easily accessible place.	Maintains current requirements.
Information or Materials Related to Oversight	Six years from the end of the fiscal year a rule 17a-7 transaction occurred, two in an easily accessible place.	Similar to current requirements, but would generally relate to the CCO's oversight requirements, specifically including

	Record relates to the board's oversight.	information or materials: (1) used to determine that each condition of the rule was satisfied for each cross trade as part of quarterly reviews; ¹ and (2) used to determine whether a cross trade, or pattern of trades, may have disadvantaged the registered fund, including information or materials related to other transactions or information reviewed as part of annual reviews. ² Records of the CCO's reports to the fund's board would also be required. ³
Notes: ¹ See proposed rule 17a-7(c)(2). ² See proposed rule 17a-7(c)(3). ³ See proposed rule 17a-7(c)(4). See <i>supra</i> section II.E for discussion of the CCO's oversight requirements.		

The proposed amendments to the recordkeeping requirements would remove duplication and correspond with other proposed amendments to rule 17a-7. The amendments are designed to ensure accountability, transparency, and verifiability for compliance and oversight purposes. The recordkeeping amendments also would allow the Commission and its staff to better understand cross-trading activities, identify issues, and conduct examinations. These amendments are designed to prevent overreaching and help address conflicts of interest that may harm investors and should improve the Commission's ability to oversee the industry and increase investor protection.

The proposal would remove the requirement to maintain and preserve permanently a written copy of the registered fund's cross-trading procedures from rule 17a-7(g)(1). This change

would remove duplication with the requirements of rule 38a-1 under the Investment Company Act, which requires registered funds to maintain a copy of their policies and procedures reasonably designed to prevent violation of the Federal securities laws that are in effect or were in effect at any time during the last five years.¹²⁶ The requirements of rule 38a-1 apply to cross trades under rule 17a-7, making rule 17a-7(g)(1) unnecessary. In addition to harmonizing the recordkeeping requirements to rule 38a-1, the proposed change would reduce recordkeeping burdens while still providing the Commission’s examination staff sufficient information to assess whether the fund is adhering to rule 17a-7 and in identifying weaknesses in compliance with the rule.

Consistent with the current rule, registered funds would be required to maintain and preserve written records of cross trades for at least six years, starting from the end of the fiscal year when the transaction took place, with the records stored in an easily accessible place for the first two years. The proposed amendments would include records on each cross trade, including a description of the security purchased or sold, the identity of the eligible affiliate on the other side of the transaction, and the terms of the purchase or sale transaction.¹²⁷

As discussed above, the current rule requires maintaining and preserving records the board used to determine, no less frequently than quarterly, that all cross trade purchases or sales made during the preceding quarter were effected in compliance with the registered fund’s cross-

¹²⁶ Rule 38a-1(d)(1).

¹²⁷ See proposed rule 17a-7(c)(1). The proposed amendment references the proposed newly defined term, “eligible affiliate,” to more clearly reference the counterparty to the cross trade rather than “the person” as used in the current rule. This will also facilitate verification that the counterparty meets the “eligible affiliate” definition.

trade procedures.¹²⁸ The proposed amendments would remove this requirement and instead require maintaining and preserving records of the information or materials upon which the CCO, rather than the board, based the determinations for the required quarterly and annual reviews.

With respect to quarterly reviews, the proposed amendments would require maintaining and preserving information or materials the CCO used to determine that each condition under the rule was satisfied with respect to each transaction, as well as the quarterly reports provided to the board on the results of those reviews.¹²⁹ The proposed recordkeeping requirement connected to the quarterly review would require, at a minimum, documentation showing whether the cross trades complied with each condition under proposed rule 17a-7.¹³⁰ Accordingly, the proposed records would need to include documentation used to determine that:

- Each security was eligible to be cross traded, for example, whether it was a level 1 or level 2 security;
- Each cross trade met the pricing condition under the proposed rule, including whether NAV pricing or current market pricing was used and, if current market pricing, how the adviser determined that the price reasonably represented current market price for the

¹²⁸ Current rule 17a-7(g)(2).

¹²⁹ See *supra* section II.E. Proposed rule 17a-7(b)(7) would require the registered fund's CCO to review, and report to the board the results of the review, (1) no less frequently than quarterly all transactions during the preceding quarter that were effected under this section to determine their compliance with rule 17a-7, and (2) no less frequently than annually all transactions during the preceding period that were effected under rule 17a-7, as well as other transactions by the fund or information necessary to evaluate transactions effected under rule 17a-7 (including the timing and price of any subsequent sales of securities purchased in cross trades), to determine whether any such transaction, or pattern of transactions, may have disadvantaged the fund relative to the eligible affiliate(s).

¹³⁰ See proposed rule 17a-7(c)(2).

cross-traded security, for example, by identifying any unaffiliated pricing source, and the results of the adviser's review of the reasonableness of those prices;

- Any fees paid in connection with the cross trade were *de minimis* and consistent with the rule;
- Each cross trade was consistent with the registered fund's policies and investment strategies; and
- The investment adviser determined the cross trade to be in the best interest of the fund, including the factors considered, such as the characteristics of the securities (*e.g.*, availability, price, and liquidity) and expected effect of the cross trade on the fund (*e.g.*, cost savings and performance).

With respect to annual reviews, the registered fund also would be required to maintain and preserve records of the information or materials the CCO used to determine whether a cross trade, or pattern of cross trades, may have disadvantaged the fund relative to eligible affiliates as part of its annual review.¹³¹ That would include information or materials related to other transactions or information necessary to evaluate those cross trades, including, as is consistent with the oversight requirement in the proposal, documentation showing that the CCO considered the timing and price of subsequent sales of securities purchased in cross trades. As part of this requirement to consider the timing and price of these subsequent sales, the fund must maintain and preserve records that detail the economic terms of each sale of a security that was purchased by a registered fund in a cross trade, including:

¹³¹ See proposed rule 17a-7(c)(3).

- The date of purchase,
- The purchase price,
- The date of the sale, and
- The sale price.

While registered funds are already required to maintain and preserve these trade records under either current rule 17a-7 or rule 31a-1, the proposal would require the CCO to review these records as part of the annual review in a manner that may not currently be done. These records also would be required to be made available to the board promptly upon request. Reports and other information provided to the board should be in a format that is easy to digest to facilitate the board's oversight.

In addition, the information or materials used in connection with the CCO's annual review that must be maintained and preserved may include, for example, information and reports that identify other details of cross-traded securities (including how prices were calculated for sales of securities acquired at different times and at different prices (*e.g.*, average price mechanics)), analysis of performance of the cross-traded security, analysis of market and fund flow conditions around the time of the cross trade, and other analyses to determine why the timing and disposition of the cross-traded security did not disadvantage the fund. The registered fund also would be required to maintain and preserve the reports the CCO provided to the board with the results of the CCO's quarterly and annual reviews.¹³²

¹³²

See proposed rule 17a-7(c)(4).

The proposed amendments do not otherwise prescribe how a fund would meet these recordkeeping requirements. These records, for example, may consist of spreadsheets or logs with dropdown lists as well as longer descriptions. The recordkeeping requirements are designed to assist the CCO's reviews and reports, help determine and test compliance with rule 17a-7, and provide important information about cross trades to the Commission and its staff.

We request comments on the proposed recordkeeping requirements:

62. Are the proposed recordkeeping requirements appropriate?

63. Should we provide more guidance or more detailed provisions in the rule on what type of records are required? If so, what should the records be required to include? Is it appropriate to require records on the CCO's determinations that cross trades were made in compliance with proposed rule 17a-7 and that a cross trade, or pattern of cross trades, did not disadvantage the fund relative to the eligible affiliate(s)? Should we provide more details in the rule or guidance on what records would show that the CCO reviewed the cross trades and other transactions or information necessary to evaluate transactions effected under this section (including the timing and price of any subsequent sales of securities purchased in cross trades)? Should the rule instead impose independent recordkeeping requirements with respect to each condition of the rule? What recordkeeping systems would need to be involved?

64. Should the rule require a particular format or contents of the documentation required to be maintained under this new requirement?

65. Are the proposed retention periods sufficient to evidence compliance? Should we require a longer (*e.g.*, eight years) or shorter (*e.g.*, four years) retention period?

66. Do registered funds have concerns that it would be difficult to maintain and preserve these records?

H. Other Amendments

We are proposing to add definitions of the terms “fund” and “eligible affiliate” to rule 17a-7 to refer to the registered funds that are permitted to rely on the rule and the types of affiliates that they can cross trade with under the rule.¹³³ We are proposing these definitions to improve the clarity of the rule, but we do not intend for the definitions to change the scope of the current rule.

Under the proposal, “fund” would mean a registered investment company, including any separate series thereof. This definition would replace language in the current rule referring to a registered investment company or a separate series of a registered investment company.

We are proposing to define “eligible affiliate” to mean, with respect to a fund:

- Another fund that is an affiliated person, or an affiliated person of an affiliated person, of such fund; and
- A person that is an affiliated person, or an affiliated person of an affiliated person, of the fund solely by reason of having a common investment adviser, investment advisers that are affiliated persons of each other, common directors, and/or common officers.

¹³³ We also propose to add a definition of the term “unaffiliated,” which is a term used in the proposed current market pricing approach with respect to unaffiliated pricing sources and in the proposed condition related to certain *de minimis* payments to unaffiliated parties. We discuss the proposed definition of “unaffiliated” in sections II.B.2 and II.C.

The “eligible affiliate” definition would replace language in the current rule referring to transactions between registered investment companies or separate series of registered investment companies, which are affiliated persons, or affiliated persons of affiliated persons, of each other, between separate series of a registered investment company, or between a registered investment company or a separate series of a registered investment company and a person which is an affiliated person of such registered investment company (or affiliated person of such person) solely by reason of having a common investment adviser or investment advisers which are affiliated persons of each other, common directors, and/or common officers. This proposed amendment would be a non-substantive change.

We request comment on the proposed definitions:

67. The proposed terms “fund” and “eligible affiliate” are intended to more clearly provide the scope of funds that currently may rely on rule 17a-7 and the scope of affiliated arrangements for which the rule currently provides an exemption. Do the proposed defined terms provide clarity relative to the current rule without changing the scope of funds or affiliated arrangements that are covered?

68. The current rule and the proposed rule refer to registered investment companies generally but include conditions related to an investment company’s board of directors that UITs could not meet, because UITs do not have boards of directors. To recognize that UITs cannot meet the conditions of the rule, should we amend the scope of rule 17a-7 to refer only to management investment companies? Are there circumstances in which UITs would benefit from being able to rely on rule 17a-7? Should we address how UITs could comply with the proposed rule’s requirements related to boards of directors and

investment advisers? For example, should a UIT's trustee, underwriter, or depositor fulfill the board-related obligations in the rule? Should a UIT be required to have an officer of the fund, or the fund's CCO, fulfill the adviser-related obligations in the proposed rule?

I. Existing Staff No-Action Letters and Other Staff Statements

We are aware that staff have previously expressed views on topics covered by the proposed amendments. For the avoidance of doubt, to the extent the proposed amendments are adopted, the Commission's views on such topics would control and any inconsistent staff views would be superseded.

Letters and statements identified as expressing staff views on topics addressed by the proposed amendments are listed below. This list may or may not be exhaustive. Commenters may name any additional staff letters or statements they identify as addressing topics covered by the proposed rule in their comment letters, particularly to the extent such letters or statements express views inconsistent with the amendments as proposed.

- Independent Directors Council, SEC Staff No-Action Letter (Oct. 12, 2018) (with respect to rule 17a-7)
- Independent Directors Council and Mutual Fund Directors Forum, SEC Staff Letter (Nov. 2, 2010) (with respect to rule 17a-7)
- ING Series Fund, Inc., et al., SEC Staff No-Action Letter (Apr. 30, 2008)
- Old Mutual Advisor Funds, SEC Staff No-Action Letter (Nov. 16, 2007)
- Gartmore Variable Insurance Trust, SEC Staff No-Action Letter (Dec. 29, 2006)
- Guidestone Financial, et al., SEC Staff No-Action Letter (Dec. 27, 2006)

- Federated Municipal Funds, SEC Staff No-Action Letter (Nov. 20, 2006)
- Citigroup Global Markets Inc., SEC Staff No-Action Letter (Sept. 26, 2006)
- GE Institutional Funds, SEC Staff No-Action Letter (Dec. 21, 2005)
- Signature Financial Group, Inc., SEC Staff No-Action Letter (Dec. 28, 1999)
- DFA Investment Trust Company, SEC Staff No-Action Letter (Mar. 21, 1996)
- DFA Investment Trust Company, SEC Staff No-Action Letter (Oct. 17, 1995)
- United Municipal Bond Fund, SEC Staff No-Action Letter (Jan. 27, 1995)
- Federated Investors, SEC Staff No-Action Letter (Apr. 21, 1994)
- United Municipal Bond Fund, SEC Staff No-Action Letter (July 30, 1992)
- TrustFunds Institutional Managed Trust, SEC Staff No-Action Letter (July 20, 1988)
- Fidelity Management & Research Co., SEC Staff No-Action Letter (June 13, 1988)
- United Services Funds, SEC Staff No-Action Letter (May 27, 1987)
- American Medical Association Retirement Plan, SEC Staff No-Action Letter (Jan. 15, 1987)
- Principal Preservation Tax-Exempt Fund, Inc., SEC Staff No-Action Letter (Nov. 6, 1986)
- Metropolitan Series Fund, Inc., SEC Staff No-Action Letter (Aug. 29, 1986)
- Benham California Tax-Free Trust and Benham National Tax-Free Trust, SEC Staff No-Action Letter (Aug. 6, 1986)

- First National Bank of Chicago, SEC Staff No-Action Letter (Feb. 5, 1986)
- Cash Accumulation Trust and Daily Accumulation Fund, SEC Staff No-Action Letter (Nov. 30, 1984)
- Lincoln National Investment Management Company, SEC Staff No-Action Letter (Apr. 25, 1976)

J. Transition Period

We propose to provide a tiered transition period for registered funds to come into compliance with the proposed amendments to rule 17a-7 and Forms N-PORT and N-MFP, if adopted, based on fund size. We propose to provide a 12-month transition period for larger entities and an 18-month transition period for smaller entities. For these purposes, larger entities would be registered funds that, together with other investment companies in the same “family of investment companies” (as such term is defined in Item B.5 of Form N-CEN), have net assets of \$10 billion or more as of the end of the most recent fiscal year. Smaller entities would be registered funds that, together with other investment companies in the same family of investment companies, have net assets of less than \$10 billion as of the end of the most recent fiscal year.¹³⁴

¹³⁴ This \$10 billion threshold is designed to be a reasonable means of distinguishing larger and smaller entities for purposes of tiered compliance dates for the proposed requirements. We estimate that, as of December 2025, 0.5% of registered investment companies would be considered to be smaller entities. These smaller entities hold approximately 0.003% of aggregate assets of registered investment companies. These estimates of smaller entities are derived from an analysis of data obtained from Morningstar Direct and data reported to the Commission (*e.g.*, Form N-PORT, Form N-CSR, Form 10-Q, and Form 10-K) for the quarter ended December 2025. The Commission also recently proposed similar amendments to its definition of “small entity” for purposes of the Regulatory Flexibility Act for investment companies. See Amendments to the “Small Business” and “Small Organization” Definitions for Investment Companies and Investment Advisers for Purposes of the Regulatory Flexibility Act, Investment Company Act Release No. 35864 (Jan. 7, 2026) [91 FR 1107 (Jan. 12, 2026)] (“Small Entity Proposing Release”).

Under the proposed approach, a registered fund's cross trades would be subject to the conditions of the amended rule at the end of the transition period. Prior to that time, cross trades would be subject to the current rule's conditions. Similarly, funds would be required to report information about their aggregate cross trades on Form N-PORT or Form N-MFP, as applicable, for the next report that is filed after the transition period ends. The tiered transition period is designed to provide registered funds with time to adjust their oversight processes, policies and procedures, and reporting and recordkeeping infrastructure to comply with the amendments. Notwithstanding the tiered transition period, registered funds would be permitted to voluntarily comply with the amendments in advance of the relevant compliance date. To promote regulatory consistency, however, any registered fund that elects to rely on the amended rules prior to compliance date must rely on the rules as amended in their totality.

We request comment on the proposed transition period.

69. Would the proposed transition period provide registered funds enough time to comply with the proposed amendments? Should the period be shorter or longer?

70. Should the transition period differ by fund size, as proposed, or should the transition period be the same for all registered funds? Is there a different approach we should use for determining fund size for purposes of the transition period?

III. ECONOMIC ANALYSIS

A. Introduction

The proposed amendments would expand the types of securities eligible for cross trades to include securities valued using observable level 2 inputs, provide two pricing options (NAV-based pricing or current-market pricing using one or more unaffiliated pricing sources),

reallocate certain oversight responsibilities from the board to the fund's CCO through quarterly and annual reviews, and permit only *de minimis* payments to unaffiliated parties for necessary administrative services such as clearing and settlement. The amendments would also update recordkeeping requirements and add new structured reporting on Forms N-PORT and N-MFP requiring registered funds that engage in cross trades to report monthly cross-trade activity and aggregate purchase and sale activity by asset class.

As discussed above, cross trading is prohibited under section 17(a). Examples of problematic practices include parking,¹³⁵ cherry-picking,¹³⁶ and dumping¹³⁷ securities between a registered fund and its affiliates. However, in circumstances where those conflicts can be effectively mitigated, economic theory suggests that internal execution can achieve the same allocative result as external execution, while consuming fewer real resources.¹³⁸ When a registered fund and its eligible affiliate have offsetting trading interest and a security can be reliably valued through independent pricing, dealer-intermediated execution (that is, execution routed externally through a broker-dealer acting in a principal or agency capacity) may not add any additional benefits to the transaction for either counterparty. Yet dealer intermediation requires greater consumption of real resources, including dealer labor, operational infrastructure,

¹³⁵ See *supra* note 37 and accompanying text.

¹³⁶ See *supra* note 38 and accompanying text.

¹³⁷ See *supra* note 39 and accompanying text.

¹³⁸ This paragraph describes the economic mechanism through which cross trades can reduce real resource use. Later sections of the economic analysis discuss additional economic effects that may arise under different trading conditions, including cases involving conflicts of interest, valuation dispersion, or timing differences.

settlement processes, and adviser search costs. Under the current regulatory definition of readily available market quotations, level 2 securities generally cannot be cross traded. As a result, advisers must route trades through external intermediaries even in cases where an internal match could achieve a better economic outcome.¹³⁹ From a social-welfare perspective, this represents a productive inefficiency.

When accounts engage in a cross trade, the price reflects a single valuation derived from reliable, market-based inputs. If both sides have offsetting interest and rely on that same market-informed value, routing the trade externally would not add any meaningful price-setting or negotiation function. In such cases, dealer involvement can introduce additional transaction costs without altering the economic terms of the trade.

Permitting cross trading in level 2 securities under appropriate safeguards (independent valuation, conflict-of-interest controls, and CCO and board oversight) would allow advisers to use the more efficient execution method subject to conditions designed to protect the interests of each fund and its shareholders.

Cross trading may allow funds and certain affiliates to lower trading costs, avoid unnecessary market impact, and match complementary trading needs more effectively than in external markets. At the same time, cross trading can harm funds or other clients and create conflicts of interest because the adviser acts on behalf of multiple funds and affiliates whose

¹³⁹ Although internal execution could in principle reduce transaction costs for level 3 securities as well, such savings do not permit any inference about welfare effects because level 3 valuations rely on unobservable inputs and adviser-specific modeling rather than market-generated price signals. Without observable inputs anchoring the price, an internal cross trade cannot be assumed to replicate the allocative efficiency of a market transaction. As a result, the welfare implications of internalizing trades in level 3 securities are inherently indeterminate, even apart from conflicts of interest.

interests might not always align.¹⁴⁰ As explained in section I.C, additional conflicts may also arise when an adviser’s compensation varies across the participating funds or affiliates, for example, when advisory or performance-based fees differ, or when the adviser or its personnel have financial interests connected to an affiliate. Without appropriate safeguards, a registered fund could be disadvantaged relative to an affiliate.¹⁴¹ The proposed amendments therefore would provide conditions, such as eligibility limits, pricing requirements, fee restrictions, adviser best-interest determinations, and structured CCO oversight, to help funds capture these efficiencies while mitigating conflicts.

The Commission considered the potential economic effects of the proposed amendments to rule 17a-7 and the new Form N-PORT and Form N-MFP reporting requirement associated with these amendments, including the anticipated benefits and costs to registered investment companies, investment advisers, fund boards, and investors. To assess these effects, the economic analysis evaluates the proposed amendments relative to the current regulatory and market baseline. Accordingly, the discussion first describes the baseline, then examines the

¹⁴⁰ See, e.g., Gerald Abdesaken, *Conflicts of Interest in Multi-Fund Management*, 20 J. ASSET MGMT. 54 (2019) at 54–56, which identifies multi-fund management as a source of “agency conflict” and shows that coordinated opposite-trading can advantage some funds at the expense of others, illustrating how cross trading can create principal–agent concerns when an adviser represents multiple funds with potentially divergent interests.

¹⁴¹ Several studies document that, without adequate safeguards, internal trades can advantage one affiliated fund while disadvantaging another. Eisele et al. (2020) find that cross trades may be used to “opportunistically reallocate performance among trading funds,” suggesting that value can be shifted between funds when monitoring is weak. Alexander Eisele et al., *Trading Out of Sight: An Analysis of Cross-Trading in Mutual Fund Families*, 135 J. FIN. ECON. 359 (2020); Gaspar et al. (2006) likewise show that certain funds within a family “overperform at the expense of” others, with coordinated opposite-signed trades contributing to these distributional effects. Jose-Miguel Gaspar et al., *Favoritism in Mutual Fund Families? Evidence on Strategic Cross-Fund Subsidization*, 61 J. FIN. 73 (2006); Abdesaken (2019) similarly finds that managers “cross-subsidize top performing funds at the expense of low performing funds” through cross- or opposite-trading activity, underscoring the potential for harm to one fund if protections are insufficient. Abdesaken, 20 J. ASSET MGMT. 54.

expected benefits and costs of the proposed amendments, then considers the potential effects on efficiency, competition, and capital formation, and finally evaluates the potential economic effects of certain reasonable alternatives. Many of these economic effects are difficult to quantify; where quantification is not practicable, the Commission instead provides a qualitative discussion of the potential economic consequences.

B. Baseline

This section describes the existing regulatory framework, entities involved in cross trading of securities, and current market practices under the existing rule. Consistent with the SEC's guidance on economic analysis in rulemaking,¹⁴² this baseline serves as the reference point against which the likely economic effects of the proposed amendments can be evaluated.¹⁴³

1. Regulatory Framework

Section 17(a) of the Investment Company Act generally prohibits certain transactions between a registered investment company and its affiliates, such as the sale or purchase of securities unless an exemption applies, or the transaction is otherwise permitted by SEC rules. Specifically, it is unlawful for an affiliated person (or an affiliate of such a person), acting as

¹⁴² SEC Division of Risk, Strategy & Financial Innovation & Office of the General Counsel, *Current Guidance on Economic Analysis in SEC Rulemakings* (Mar. 16, 2012), available at https://www.sec.gov/divisions/riskfin/rsfi_guidance_econ_analy_secrulemaking.pdf.

¹⁴³ See, e.g., *Nasdaq v. SEC*, 34 F.4th 1105, 1111-14 (D.C. Cir. 2022). This approach also follows Commission staff guidance on economic analysis for rulemaking. See SEC Staff, *Current Guidance on Economic Analysis in SEC Rulemaking* (Mar. 16, 2012), available at https://www.sec.gov/divisions/riskfin/rsfi_guidance_econ_analy_secrulemaking.pdf (“The economic consequences of proposed rules (potential costs and benefits including effects on efficiency, competition, and capital formation) should be measured against a baseline, which is the best assessment of how the world would look in the absence of the proposed action.”); *id.* at 7 (“The baseline includes both the economic attributes of the relevant market and the existing regulatory structure.”).

principal, to sell any security or other property to the investment company or purchase any security or other property from the investment company unless permitted by rule or exemption.¹⁴⁴

Rule 17a-7 provides a narrow exemption for certain purchase or sale transactions between investment companies and certain affiliates.¹⁴⁵ To qualify for the exemption under current rule 17a-7, the transaction must meet the following conditions: (1) The security involved must have market quotations that are readily available;¹⁴⁶ (2) The transaction must be executed at the independent current market price;¹⁴⁷ (3) The transaction must align with the investment policies of each participating fund, as disclosed in their registration statements and reports;¹⁴⁸ (4) No brokerage commission, fee, or other remuneration may be paid, except for customary transfer fees;¹⁴⁹ (5) The fund's board of directors, including a majority of disinterested directors, must adopt written procedures reasonably designed to ensure compliance with the rule; review and approve any changes to those procedures, and determine at least quarterly that all transactions

¹⁴⁴ 15 U.S.C. 80a-17(a). Note that section 17(a) applies only to transactions effected "knowingly," meaning the affiliated person must have actual knowledge or intent to engage in the prohibited transaction. Inadvertent or unintentional trades, if made in good faith, may not constitute a violation.

¹⁴⁵ 17 CFR 270.17a-7 - Exemption of certain purchase or sale transactions between an investment company and certain affiliated persons thereof.

¹⁴⁶ 17 CFR 270.17a-7(a). The transaction also must be for no consideration other than cash payment against prompt delivery of the security.

¹⁴⁷ 17 CFR 270.17a-7(b). The rule provides a detailed hierarchy for determining this price. For National Market System (NMS) stocks, the last sale price or the average of the highest independent bid and lowest independent offer. For exchange-traded but non-reported securities, the last sale or bid/offer average on the exchange. For NASDAQ-quoted securities, the average of the highest bid and lowest offer on Level 1 of NASDAQ. For all other securities, the average of the highest current independent bid and lowest offer based on reasonable inquiry.

¹⁴⁸ 17 CFR 270.17a-7(c).

¹⁴⁹ 17 CFR 270.17a-7(d).

were executed in accordance with the procedures;¹⁵⁰ (6) The board must meet the governance standards defined in rule 0-1(a)(7), which include requirements for board composition and independence;¹⁵¹ and (7) The registered fund must permanently maintain a written copy of the procedures and any modifications; maintain detailed records of each transaction for at least six years (with the first two years in an easily accessible place), including a description of the security, the identity of the counterparty, terms of the transaction, and supporting documentation for the board's quarterly determinations.¹⁵²

Funds are also subject to existing requirements under rule 38a-1, which require them to adopt written compliance policies and procedures reasonably designed to prevent violation of the Federal securities laws, require CCO and board oversight, and require them to maintain related records. Although these requirements are not specific to cross trading, they require funds to have policies and procedures reasonably designed to prevent violations of section 17(a) of the Investment Company Act through cross trades that do not comply with rule 17a-7, to review the effectiveness of the policies and procedures at least annually, and report to the board at least annually. As a result, under the current regulatory framework funds already generate and maintain materials relating to compliance policies and procedures and reviews, and the proposed amendments would expand the amount of documentation required to be maintained by funds insofar as the new quarterly and annual cross-trade reviews interact with these existing obligations.

¹⁵⁰ 17 CFR 270.17a-7(e).

¹⁵¹ 17 CFR 270.17a-7(f).

¹⁵² 17 CFR 270.17a-7(g).

In the 1990s and early 2000s, Commission staff issued several no-action letters addressing cross trading of municipal securities in circumstances where market quotations were not readily available, stating that staff would not recommend enforcement action related to the use of evaluated prices under specific conditions.¹⁵³ Separately, in 2018, the staff stated it would not recommend enforcement action if a fund’s board received a written representation from the fund’s CCO that transactions effected in reliance on rule 17a-7 complied with the board-approved procedures, rather than the board itself making that determination.¹⁵⁴ These staff positions do not reflect Commission rules and do not alter the requirements of rule 17a-7, but they may inform aspects of current industry practice to the extent advisers acted consistent with such staff positions.

Rule 2a-5, adopted in 2020, defined “readily available market quotations” to include only unadjusted quoted prices in active markets for identical securities.¹⁵⁵ Aligned with level 1 inputs under ASC 820,¹⁵⁶ this definition excluded evaluated prices, matrix pricing, and non-public or indicative broker-dealer quotes. As a result, fixed-income securities that previously were cross traded under rule 17a-7 generally became ineligible for cross trading.

In addition to rule 17a-7 under the Investment Company Act, cross trading is also subject to section 206(3) of the Advisers Act, which prohibits investment advisers from engaging in

¹⁵³ See, e.g., United No-Action Letter; Federated No-Action Letter.

¹⁵⁴ See IDC No-Action Letter.

¹⁵⁵ 17 CFR 270.2a-5(c) (defining “readily available market quotations”).

¹⁵⁶ See ASC 820 - Fair Value Measurement, which defines level 1 inputs as “quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity can access at the measurement date.”

principal or agency cross transactions without disclosing the conflict and obtaining the client’s consent.¹⁵⁷ In addition, an adviser’s fiduciary duty under the Advisers Act, including its duty of care and duty of loyalty, applies to cross-trading decisions and requires advisers to seek best execution for each client and act in the best interest of each client when determining whether a cross trade is appropriate.

In addition to funds, BDCs may also engage in or be affected by cross trades. BDCs are subject to restrictions on affiliated transactions, including cross trades, under section 57 of the Investment Company Act. Section 57(i) of the Investment Company Act generally provides that rules under section 17(a) apply to BDCs until the Commission adopts corresponding rules under section 57, which has not occurred. Because rule 17a-7 applies to transactions between a registered fund and any “affiliated person” or an “affiliated person of an affiliated person”—including persons affiliated solely through a common investment adviser—registered funds may also cross trade with private funds or other accounts advised by the same adviser, provided all rule 17a-7 conditions are satisfied.¹⁵⁸

2. Affected Entities

The affected population for this rule consists of registered funds and other accounts that qualify as eligible affiliates. As of December 2025, there were 14,297 registered funds managing

¹⁵⁷ See section 206(3) of the Advisers Act (principal and agency cross-transaction prohibition).

¹⁵⁸ Rule 17a-7 expressly permits cross trades between a registered investment company and any “affiliated person” (or an affiliated person of such a person), including a person that is an affiliate solely by reason of having a common investment adviser. 17 CFR 270.17a-7(a).

\$47 trillion in total net assets (TNA).¹⁵⁹ Table 2 shows the number of registered funds and TNA, by fund category, as of December 2025, based on Form N-CEN data and Form 10-K filings and related amendments. Mutual funds were the largest category of funds, accounting for 8,516 funds and \$29.9 trillion in TNA. ETFs represented the second-largest category with 4,194 funds with about \$13.0 trillion in TNA. Together, mutual funds and ETFs made up 89% of total fund count and 91% of the total net asset base. The remaining fund types collectively represent a small but meaningful share of the market. Closed-end funds account for 707 funds with \$428 billion in assets, while the management company separate accounts (MCSAs) comprise 15 funds totaling \$279 billion. UITs represent another 693 funds with \$3.0 trillion in TNA,¹⁶⁰ and BDCs include 171 funds with roughly \$235 billion in assets. There were two face amount certificate companies (FACCs) as of December 2025.¹⁶¹ Among investment advisers reported on Form N-CEN as of December 2025, approximately 300 advisers reported advising multiple clients on Form ADV for the same period. Under rule 17a-7, a registered fund may engage in cross trades only with

¹⁵⁹ Form N-CEN data, reporting period ending December 2025 with filings received through March 31, 2026. The numbers of BDCs and FACCs were based on Form 10-K filings and related amendments in calendar year 2025.

¹⁶⁰ UITs are included in the baseline as part of the universe of registered investment companies, even though they do not have boards and therefore cannot rely on rule 17a-7.

¹⁶¹ Mutual funds are registrants that file on Form N-1A, excluding ETFs. Some mutual funds have an ETF share class. For purposes of the data presented, these filers are reported in the ETF category rather than in the open-end mutual fund category. This presentation avoids double-counting mutual fund registrants that offer both mutual fund and ETF share classes. Closed-end funds represent Form N-2 filers that are not classified as BDCs. MCSAs refer to management company separate accounts registered on Form N-3 that offer variable annuity insurance products. UIT counts include filers under Forms N-4, N-6, N-8B-2, and S-6. BDCs and FACCs are based on Form 10-K filings and related amendments in calendar year 2025.

affiliated persons whose affiliation arises solely for the reasons specified in the rule, such as when two advisory clients share the same adviser.¹⁶²

Table 2: Fund Counts and Total Net Assets by Fund Category (As of December 2025)

Category	Fund Count	TNA (\$ Billions)
Mutual Funds	8,516	29,935
Exchange-Traded Funds (ETFs)	4,194	12,960
Closed-End Funds	707	428
MCSA	15	279
UITs	693	3,047
BDCs	171	235
FACCs	2	-
Total	14,297	46,884

Source: Form N-CEN Items C.19, F.11, and F.14. The value for total net assets is the sum of monthly average total net assets for mutual funds and ETFs, daily average total net assets for money market funds, and total assets for UITs. The ETF counts include mutual funds that offer at least one ETF share class, and the total net assets of ETFs include the assets of those mutual funds. BDC asset information was obtained from issuers' 2025 Form 10-K filings and related amendments. FACCs issue face-amount certificates rather than fund shares and do not maintain a net asset value comparable to other registered fund types; accordingly, no TNA figure is reported for FACCs in Table 2.

Form N-CEN filings for fiscal years ending in 2025 show 303 registered fund families. Of these, 21 fund families (about 7%) reported only one active fund, and therefore would be unlikely to engage in cross trades between two registered funds under rule 17a-7, which requires that the funds be affiliated (for example, by being under common control or sharing the same investment adviser). The remaining 282 families (about 93% of registered fund families) had two

¹⁶² Eligible affiliates may include any advisory client whose affiliation with the registered fund arises solely because they share a common investment adviser (or affiliated advisers), common directors, or common officers, as specified in rule 17a-7. These advisory clients may include private funds, separately managed accounts ("SMAs"), ERISA plans, and other institutional clients; however, many private funds and other clients may not satisfy the "solely" condition because the adviser or its affiliate may have an economic interest in those clients, or those clients may otherwise be affiliated with a regulated fund in ways beyond those specified in rule 17a-7. We therefore identify advisory clients advised by the same adviser for context, but do not assume they are eligible affiliates. Compliance with rule 17a-7 would not relieve a party engaging in a cross trade involving an ERISA plan from complying with applicable ERISA provisions.

or more funds, and thus potentially greater opportunity to conduct cross trades between affiliated funds.¹⁶³

The potential for cross trades increases with the number of funds that are part of a fund family as well as the degree to which the holdings or investment strategies of affiliates overlap. Form N-CEN data for funds whose fiscal year ended during 2025 shows that the top five investment advisers collectively managed 1,611 funds with aggregate average total net assets of approximately \$23 trillion. However, shared advisory relationships do not necessarily imply that cross trading occurs. Funds managed by the same adviser may belong to different fund families, each with their own compliance policies and operational procedures. These differences may limit cross trading in practice, even when it might otherwise benefit a fund and an affiliate that share an adviser.

Annual Form N-CEN fund-level data for fiscal year-end 2025 shows 2,294 funds reported reliance on rule 17a-7 in their regulatory filings,¹⁶⁴ meaning that they maintained the capacity and procedures to engage in affiliated cross trades under the rule, if and when appropriate. These funds represent the universe of entities that could have engaged in such transactions, although additional funds may choose to cross trade under the proposed amendments.

¹⁶³ Form N-CEN, Items B.5, and B.6, period ending December 2025 with filings received through March 31, 2026.

¹⁶⁴ Form N-CEN, Item C.9 – Excluding sub-advisers and terminated advisers. This figure reflects the number of funds/series estimated to rely on proposed rule 17a-7. The number of registrants that may rely on the rule will differ.

Beyond cross trades between registered funds, persons responding to the Staff Statement explained that¹⁶⁵ large advisers may also conduct cross trades between a registered fund and other client accounts—including separately managed accounts, pension plans, insurance portfolios, and UCITS¹⁶⁶—when those accounts hold the same securities as affiliated funds. These other accounts typically trade with registered funds under common management and generally participate only when those accounts have complementary buy-and-sell interest in the same securities. One letter also provided information about equity cross-trading activity, noting that such trades likewise most often occur between registered funds but may also involve these other adviser-managed accounts when those accounts have offsetting trading interest in the same securities.¹⁶⁷ Although these non-RIC accounts represent a smaller share of potential cross-trading volume than registered funds, they can increase internal matching opportunities in complexes with substantial trading activity.

An SEC staff analysis¹⁶⁸ of corporate and municipal bond holdings using Form N-PORT and Form N-CEN filings, indicates that affiliated bond cross-trading activity is primarily undertaken by large, multi-fund investment complexes with substantial fixed-income operations.

¹⁶⁵ See, e.g., PIMCO Letter; Capital Group Letter; and Invesco Letter.

¹⁶⁶ UCITS refers to “Undertakings for Collective Investment in Transferable Securities,” a type of regulated European pooled investment vehicle that advisers may manage alongside U.S.-registered funds. Although UCITS are not registered investment companies under the Investment Company Act, they can be eligible affiliates for purposes of rule 17a-7 when advised by the same adviser.

¹⁶⁷ Investment Company Institute, *Rule 17a-7 at the Crossroads: Supplemental Information on Equity Cross Trading* (Oct. 2021), available at https://www.ici.org/system/files/2021-10/21_ppr_rule17a7_supplement.pdf.

¹⁶⁸ See Su Li, *Cross-Trading of Fixed Income Securities in U.S. Mutual Fund Families*, SEC Staff White Paper (2026) available at <https://www.sec.gov/files/dera-cross-trad-mut-fund-fam-wp-2609.pdf>. This analysis covers open-end mutual funds within the Form N-PORT/N-CEN reporting universe, excludes ETFs and registered closed-end funds, and does not include BDCs, which do not file Forms N-PORT or N-CEN.

In June cross-sections from 2020–2024, the industry contains roughly 600–700 fund families; however, only those families in which the same investment adviser (or affiliated advisers) manages multiple funds and other client accounts with active fixed-income trading—and thus recurring buy and sell interest in the same securities—tend to have practical opportunities for affiliated cross trading of fixed-income securities. Cross trading requires at least two affiliated accounts to have opposing trade interests in the same bond, a condition that occurs primarily in large complexes with deep, overlapping fixed-income holdings. The 10 largest fund families typically oversee dozens of funds and manage tens of billions of dollars in portfolio securities. Although the analysis relies solely on registered-fund data and does not capture activity in non-RIC accounts, advisers within these families that also manage non-RIC client accounts investing in similar fixed-income instruments could, in principle, encounter additional situations in which affiliated cross-trading activity might arise. These families also hold thousands of distinct corporate- and municipal-bond securities with unique CUSIPs, including families with 7,000–8,000 corporate bonds and over 30,000 municipal bonds, with multiple affiliated funds often holding the same security.

Members of the public reported that cross-trading opportunities extend beyond registered funds because advisers often manage other accounts such as institutional SMAs, insurance accounts, bank-loan portfolios, and UCITS with overlapping fixed-income holdings.¹⁶⁹ These accounts may also have offsetting buy-and-sell interest when securities are being sold to meet

¹⁶⁹ See, e.g., PIMCO Letter; Capital Group Letter; Invesco Letter.

redemptions or to satisfy index-rebalancing constraints, particularly within fixed-income ETF suites.

Investors across a variety of registered investment companies—including mutual funds, ETFs, and closed-end funds—as well as BDCs may be affected by the economic outcomes of cross-trading practices. In addition, advisers often manage other affiliated accounts—such as institutional separate accounts, insurance accounts, bank-loan portfolios, private funds, collective trusts, and UCITS—whose investors may also be affected when these accounts participate in cross-trading activity. In 2025, mutual funds were held by approximately 72.7 million U.S. households, while 19.8 million households owned ETFs, and 4.4 million households owned closed-end funds.¹⁷⁰ The typical mutual fund-owning household reported a median income of \$125,000, median financial assets of \$370,000, and \$125,000 invested in mutual funds. In comparison, ETF-owning households reported a higher median income of \$150,000 and median financial assets of \$500,000, while closed-end fund-owning households reported a median income of approximately \$125,000 and median financial assets of \$500,000.¹⁷¹

3. Market Practices

a. Eligible Assets Under Rule 17a-7

Currently, cross trades are primarily limited to securities with prices that are publicly available and easy to verify. This typically includes exchange-listed equities (such as S&P 500 stocks), U.S. Treasury securities (typically on-the-run issues with readily available market

¹⁷⁰ Investment Company Institute, *2026 Investment Company Fact Book: A Review of Trends and Activities in the Investment Company Industry*, 66th ed., available at <https://www.ici.org/system/files/2026-04/2026-factbook.pdf>.

¹⁷¹ *Id.*

quotations), and agency mortgage-backed securities (all securities that trade in active markets with transparent pricing). To quantify the scope of assets that are eligible for cross trading under rule 17a-7, Table 3 shows the aggregate gross value of assets held by mutual funds, ETFs, and closed-end funds, categorized by fair value level. Level 1 securities, which have quoted prices in active markets, are generally eligible for cross trading under rule 17a-7. Level 2 securities are typically valued using observable inputs other than quoted prices, such as quoted prices for similar assets, interest rates, yield curves, or credit spreads, and are often derived from pricing models or vendor evaluations. Level 2 securities do not meet the “readily available market quotation” standard under rule 2a-5 and therefore are typically ineligible for cross trading, although certain municipal bonds, which are often classified as level 2, have been the subject of cross trades in reliance on SEC staff no-action letters.¹⁷² Level 3 securities and non-leveled securities are valued using unobservable inputs or lack classification under the ASC 820 fair value hierarchy and are excluded from cross trading under rule 17a-7.

¹⁷² See, e.g., Federated No-Action Letter (permitting affiliated municipal-bond funds to engage in rule 17a-7 cross trades in municipal securities without readily available market quotations, based on independent pricing from SPSE or other pricing services).

**Table 3: Gross Value of Investments by Fair Value Level
(September 2025, \$ Billions)**

Fund Type	Level 1	Level 2	Other*	Total
Mutual Funds	19,388	9,015	407	28,810
ETFs	8,921	3,547	6	12,474
Closed-End Funds	160	235	242	637

Source: U.S. Securities and Exchange Commission, Division of Investment Management, Analytics Office, Registered Fund Statistics: Form N-PORT and Form N-CEN Data, period ending September 2025, Tables 9.1, 9.4, and 9.7. *available at* <https://www.sec.gov/files/investment/im-investment-registered-fund-statistics-20260129.pdf>.

* Other: Level 3 + Non-leveled (non-leveled refers to assets not classified under ASC 820 fair value hierarchy).

b. Cross-Trading Activity

No direct data on actual cross-trade executions are available; the existing available data derive from selected samples, proxy-based indicators, and industry surveys.

i. Equity Cross-Trading Activity

Several academic studies and industry surveys provide evidence on the frequency of equity cross trading among affiliated funds. A research paper found that between 1999 and 2010, a sample of 388 U.S. mutual fund families executed nearly half a million internal equity cross trades, representing 1.6% of daily trade orders (defined as the aggregation of all trades by a fund family in a given stock, on a given side (buy or sell), on a given day) and 3.1% of total trade value.¹⁷³ An academic study found that cross trades made up about 0.9% of all individual equity trade executions reported by mutual fund families in a sample of more than four million transactions from 1999 to 2010.¹⁷⁴

¹⁷³ Yue-Cheong Chan et al., *Trading by Crossing*, Asian Bureau of Finance and Economic Research (ABFER) Annual Conference (May 14, 2018), *available at* <https://abfer.org/component/edocman/main-annual-conference/trading-by-crossing>.

¹⁷⁴ Eisele et al., *supra* note 141.

An industry survey of 44 registered fund companies,¹⁷⁵ representing more than \$24.5 trillion in assets, or approximately 75% of all U.S.-registered fund assets as of July 2021, suggested that equity cross trades accounted for 1.8% of the total dollar amount of equity trading and involved about \$185 billion in cross-trade dollar volume activity by surveyed mutual funds and ETFs in 2020.¹⁷⁶

Separately, prior academic research has examined cross trading within mutual fund families, documenting that over 30% of observed equity cross trades by actively managed mutual funds involve an affiliated index mutual fund rather than another active fund on the other side of the trade. For the subset of active funds with significant holdings overlap with an affiliated index fund, greater levels of cross trading between the active fund and that index fund are associated with higher subsequent performance of the active fund.¹⁷⁷

ii. Municipal Bond Cross-Trading Activity

Available research on municipal securities suggests that affiliated fixed-income funds also cross trade, though the evidence comes from more limited sources. A research paper found

¹⁷⁵ See Investment Company Institute, *Rule 17a-7 at the Crossroads*, *supra* note 167.

¹⁷⁶ The survey reports that respondents cross traded approximately \$185 billion in equity securities in 2020. To estimate the share of overall equity trading activity represented by these cross trades, the survey adjusts this figure by double-counting trades where funds were on both sides of the transaction (to reflect both the purchase and the sale) and counting single-sided trades once, resulting in approximately \$339 billion in total cross-trading activity. Dividing this amount by the roughly \$18.5 trillion in equity trading activity reported for respondents' equity mutual funds and ETFs yields the estimate of about 1.8%.

¹⁷⁷ See Caitlin D. Dannhauser & Harold D. Spilker III, *The Modern Mutual Fund Family*, 148 J. FIN. ECON. 1 (2023), available at <https://doi.org/10.1016/j.jfineco.2023.02.001>.

that out of a sample of 7,236 affiliated municipal bond fund-pair-quarter observations, 994 (13.7%) showed cross-sales and 662 (9.1%) showed cross-buys during the period 2002-2016.¹⁷⁸

iii. Corporate and Other Fixed-Income Cross-Trading Activity

Since the adoption of rule 2a-5 in 2020, many bonds and other fixed-income securities have been excluded from cross trading because their valuations are often based on estimates or dealer quotes, which do not meet the current regulatory definition of a “readily available market quotation.”¹⁷⁹

An SEC Staff White Paper analyzing Form N-PORT data from 2019–2024 finds that affiliated fixed-income cross trading opportunities arise regularly within large fund complexes for both corporate and municipal bonds. Before the compliance date of rule 2a-5, exact-match opportunities, defined as near-exact affiliated buy-sell matches of the same CUSIP, account for roughly 0.33–1.14% of quarterly corporate-bond trades and 0.49–3.96% of traded corporate-bond volume, with a peak near 3.96% in late 2021. Overlapping opportunities (cases where affiliated funds buy and sell the same CUSIP in the same period but in different quantities) are more common, representing approximately 1.68–4.63% of corporate-bond trades and 1.96–5.24% of volume. After the rule 2a-5 compliance date, corporate-bond exact-match

¹⁷⁸ These figures reflect directional estimates of potential cross trades based on offsetting holdings changes. A fund-pair may show a cross-sale without a corresponding cross-buy, and vice versa, depending on the direction of net trades during the quarter. See Z. Jay Wang & Jingyun Yang, *Cross-Trading and liquidity management: Evidence from municipal bond funds*, 67 PACIFIC-BASIN FIN. J. 101564 (2021).

¹⁷⁹ See, e.g., Amy R. Doberman, *Cross-Trading at a Crossroads*, 32 INV. LAW. 1 (Jan. 2025) explaining that the rule 2a-5 adopting release states that “evaluated prices are not readily available market quotations” because they are not based on “unadjusted quoted prices from active markets for identical investments,” which in turn “effectively mean[s] that the only securities that could meet the standard set forth in Rule 17a-7 would be Level 1 assets.”

opportunities collapse to near zero and overlapping activity declines substantially.¹⁸⁰ In municipal securities both exact-match and overlapping opportunities remain stable throughout the sample, with exact matches representing roughly 0.91–2.08% of trades and about 1.95–2.96% of volume, and overlapping opportunities accounting for 1.66–2.45% of trades and about 2.65–5.06% of volume.¹⁸¹

A recent academic working paper examines cross trading in corporate bonds¹⁸² using two proxy-based indicators derived from mutual fund holdings changes and TRACE-reported volume.¹⁸³ The authors use these proxies solely to estimate the frequency with which trading patterns appear consistent with potential same-family crossing. The paper reports that prior to the adoption of rule 2a-5, between 4% and 6% of bond-family-quarter observations meet the proxies' criteria. Following the rule's adoption, the share of observations flagged by the unreported-volume proxy falls, while the share flagged by the offsetting-trades proxy rises modestly. The authors emphasize, however, that these indicators capture inferred patterns rather than observed internal transactions, and that their values may diverge from actual activity after the rule, either overstating or understating true crossing, because the proxies rely on indirect

¹⁸⁰ Overlapping opportunities do not fall to zero because, by construction, this measure counts any month in which affiliated funds both buy and sell the same CUSIP, regardless of whether the amounts are closely matched; as long as such independent buy and sell activity occurs within a fund complex, some overlapping observations will remain.

¹⁸¹ See Li, *Cross-Trading of Fixed Income Securities in U.S. Mutual Fund Families*, *supra* note 168.

¹⁸² See Lina Han et al., *Cross Trading in the Corporate Bond Market*, SMU Cox Sch. of Bus., Research Paper No. 25-15 (2025), available at <https://doi.org/10.2139/ssrn.5263491>.

¹⁸³ The first measure, “Off-Tape Cross,” flags cases where mutual fund trading activity inferred from holdings changes exceeds the volume reported on TRACE, suggesting unreported or internal trades. The second, “MF Cross,” identifies near-offsetting purchases and sales of the same bond by different funds within the same family during the same period, which may indicate internal matching. Both are indirect estimates and may capture different types of internal activity, not all of which are subject to rule 17a-7.

information that is sensitive to reporting practices, data limitations, and portfolio-level flows. Accordingly, the persistence of proxy-identified patterns in the post-rule period should be understood as a feature of the measurement approach, not as evidence that cross trading continued after rule 2a-5.

An industry survey of 52 registered fund complexes found that fixed-income cross trades represented approximately 3.7% of surveyed complexes' total fixed-income trading activity and involved more than \$200 billion in cross-trade dollar volume in 2020, prior to the effective date of rule 2a-5.¹⁸⁴ Survey respondents reported that these trades were primarily used for rebalancing, liquidity management, and other portfolio adjustments, particularly in markets where pricing is observable but not exchange-traded. Although the survey does not provide percentages for each category of use, the report explains that the drivers of these trades—such as continuous maturity roll-down, regular index rebalancing, credit-rating changes, and ongoing flow differences among funds—arise as part of normal, year-round portfolio management. These underlying factors suggest that the uses identified by survey respondents occur on a recurring basis rather than being episodic.¹⁸⁵

¹⁸⁴ See Investment Company Institute, *Rule 17a-7 at the Crossroads*, *supra* note 167. The survey reports that respondents cross traded more than \$200 billion in fixed-income securities in 2020. To estimate the share of overall fixed-income trading activity represented by these cross trades, the survey adjusts this figure by double-counting trades where funds were on both sides of the transaction (to reflect both the purchase and the sale), counting single-sided trades once, and excluding certain money-market instruments (such as VRDNs, commercial paper, and certificates of deposit) to align the numerator with the long-term fixed-income trading denominator. This results in approximately \$268.4 billion in adjusted cross-trading activity. Dividing this amount by the roughly \$7.3 trillion in long-term fixed-income trading reported by respondents yields the estimate of about 3.7%.

¹⁸⁵ See *id.*

Respondents explained that fixed-income cross trades tend to occur primarily within large investment complexes and are most often used for purposes such as liquidity management, index rebalancing, duration adjustments, and meeting redemptions.¹⁸⁶ These trades typically function as a routine tool—and can be particularly valuable during periods of heightened market volatility¹⁸⁷—to avoid unnecessary dealer spreads and to preserve investment opportunities when another affiliated account has offsetting buy-or-sell interest in the same security.

Industry groups also noted that, while registered funds account for most cross-trading volume, advisers may also execute cross trades between registered funds and other client accounts, provided both sides benefit, and the transactions meet applicable policies and procedures. These other client types include separately managed accounts and nonregistered pooled investment vehicles such as UCITs and private funds.¹⁸⁸

Cross trades may also reflect differing investment views across portfolio-management teams and can generate measurable transaction-cost savings, even where overall activity remains limited relative to total trading volume. In addition, index-tracking fixed-income products frequently create regular, predictable opportunities for internal matching, particularly around scheduled index rebalancing dates. Overall, fixed-income cross trading appears to be recurring but not constant, arising naturally from ongoing portfolio-management processes rather than serving as a primary trading channel.

¹⁸⁶ See, e.g., PIMCO Letter; Capital Group Letter; Invesco Letter; and SIFMA AMG Letter.

¹⁸⁷ See PIMCO Letter (“Cross trades are... an important tool for managing liquidity... particularly in volatile markets, such as the market environment that occurred in March and April 2020.”).

¹⁸⁸ See, e.g., PIMCO Letter; Capital Group Letter; Invesco Letter.

c. Pricing, Valuation, and Operational Considerations

Pricing providers support the operational feasibility of cross trading by supplying pricing data used both to assess whether a security has a readily available market quotation where supplemental pricing information is relevant and, where applicable, to price the cross trade itself. According to a staff analysis of Form N-CEN filings, for funds with fiscal year ending in 2025, over 11,000 funds reported using pricing services, with the majority relying on multiple providers. While 2,364 funds used a single pricing service, 5,685 used four or more.¹⁸⁹ Pricing services provide both real-time and end-of-day prices for actively traded securities (typically level 1), as well as evaluated prices for less liquid instruments like fixed-income securities (typically level 2), using trade data, broker-dealer quotes, and proprietary models.¹⁹⁰ The top five most frequently reported pricing providers in Form N-CEN for 2024 were Bloomberg (6,597), PricingDirect (6,108 funds), ICE Data Pricing Reference Data (5,562), S&P Global (4,828), and ICE Data Services (3,968).¹⁹¹

Funds often rely on evaluated prices, broker-dealer quotes, and pricing models, frequently obtained from third-party pricing services, as inputs to their fair value determinations when market quotations are not readily available. As a result, these securities do not have

¹⁸⁹ U.S. Securities and Exchange Commission, Division of Investment Management, *Annual Registered Investment Company Update* (May 13, 2026), Table 6.9 available at <https://www.sec.gov/files/annual-registered-investment-company-update-20260512.pdf>.

¹⁹⁰ Investment Company Institute, *Fund Valuation Under the SEC's New Fair Value Rule* 16–17 (Dec. 2021), available at <https://www.ici.org/system/files/2021-12/21-ppr-fund-valuation-primer.pdf>.

¹⁹¹ SEC Division of Investment Management, *Annual Registered Investment Company Update*, *supra* note 189, at Table 6.7.

“readily available market quotations” for purposes of rule 17a-7 and therefore may not meet the requirements for pricing cross trades under the current rule.¹⁹²

From an operational perspective, board oversight of cross trades involves coordination with compliance officers, valuation committees, and fund accountants, who support implementation, monitoring, and recordkeeping.¹⁹³

Information about cross trades is typically disclosed in financial statement notes.¹⁹⁴ While Form N-CEN requires registered management investment companies (*i.e.*, mutual funds, ETFs, and registered closed-end funds) to disclose whether they relied on rule 17a-7 during the prior year, this information is limited to a yes/no indicator and does not indicate whether any cross trades actually occurred.¹⁹⁵ There is no centralized or detailed public reporting system that shows the frequency, pricing, or counterparties of cross trades.¹⁹⁶

C. Benefits and Costs

This section analyzes the expected benefits and costs of the proposed amendments to rule 17a-7, including their likely impact on registered funds, investors, and markets. The analysis identifies the main channels through which the amendments might produce economic benefits, such as reduced transaction costs and operational efficiencies, as well as the channels through

¹⁹² See, *e.g.*, Doberman, 32 INV. LAW. 1, *supra* note 179.

¹⁹³ See *id.*; Jennifer Zordani, *A Regulatory Analysis of Cross Trading and Order Aggregation*, 5 J. INV. COMPLIANCE 53, (2004).

¹⁹⁴ 17 CFR 210.4-08(k) (general notes to financial statements).

¹⁹⁵ U.S. Securities and Exchange Commission, Form N-CEN, Item C.7(e), *available at* <https://www.sec.gov/files/formn-cen.pdf>.

¹⁹⁶ There is less information available to assess cross-trading practices of funds that do not report whether they relied on rule 17a-7 on Form N-CEN and that do not report monthly portfolio-holding information on Form N-PORT. These funds include BDCs, UITs, and FACCs.

which they could impose costs, including compliance, implementation, and data-vendor expenses. Because reliable data are limited, the discussion remains qualitative where quantification is not feasible. Where benefits or costs can be quantified, the relevant estimates are provided in section III.D. The analysis also considers potential distributional effects and highlights areas where the size of the benefits and costs may be uncertain. Because cross trading is optional, any benefits or costs discussed below would arise only to the extent a registered fund or adviser chooses to engage in cross-trading activity.

In evaluating the potential economic effects of the proposed amendments, the magnitude and timing of benefits and costs discussed below are likely to vary across registered funds and advisers of different sizes. For example, larger fund complexes are likely to have more cross-trading opportunities. In addition, larger complexes, whose valuation, technology, and compliance infrastructures tend to be more developed, may be able to update processes to comply with the proposed amendments more quickly and at lower incremental cost, while smaller registered funds may face higher fixed or upfront burdens relative to their scale. Differences in resources, systems, staffing, trading volumes, and cross-trading activity could therefore influence both how compliance costs are incurred and how any economic benefits and costs materialize over time.

In addition, different types of funds may experience the proposed amendments differently based on their existing regulatory frameworks and historical reliance on rule 17a-7. BDCs, for example, generally hold significant level 3 assets and do not file Form N-PORT.¹⁹⁷ Because level

¹⁹⁷ See *supra* note 9 for a discussion of the restrictions on affiliated transactions that BDCs are subject to.

3 assets would remain ineligible for cross trading under the proposal, the amendments may not materially expand the set of transactions available to BDCs, and are therefore less likely to confer meaningful benefits on BDCs relative to other types of funds. In addition, because BDCs do not report on Form N-PORT, they would not incur the proposal's new structured-reporting obligations. For municipal securities, the staff have not recommended enforcement action if cross trades are conducted at a price using an independent pricing service,¹⁹⁸ and the proposal would allow advisers to rely on pricing-service data as inputs under either NAV pricing or current-market pricing. Because these practices are already common in municipal cross trading, we do not expect distinct or additional costs with respect to pricing municipal-security cross trades relative to current practice.

1. Expansion of Eligible Securities to Include Level 2 Securities

Before the adoption of rule 2a-5, many registered funds cross traded fixed-income securities using broker-dealer quotes to satisfy rule 17a-7's "reasonable inquiry" requirement. Under the current rule, cross trading is permitted only for securities for which market quotations are readily available. After the adoption of rule 2a-5, this standard corresponds to securities valued using level 1 inputs because those securities have readily available market quotations as defined under rule 2a-5. As a result, some complexes discontinued cross trades in securities valued using level 2 inputs, while others continued to trade certain fixed-income securities, such

¹⁹⁸ See United Municipal Bond Fund / United Municipal High Income Fund, *SEC Staff No-Action Letter* (pub. avail. July 30, 1992), as modified (pub. avail. Jan. 27, 1995), and Federated Municipal Funds, *SEC Staff No-Action Letter* (pub. avail. Nov. 20, 2006).

as municipal bonds, based on staff no-action letters, even though such securities continued to be valued using level 2 inputs for their daily NAV processes.

Under the proposed amendments, a security would be eligible for cross trading if it has readily available market quotations or would be valued using observable inputs.¹⁹⁹ This would expressly include securities valued using level 2 inputs and would continue implicitly to exclude securities valued using level 3 inputs. As a result, the universe of securities eligible for cross trading would broaden, while preserving the existing non-inclusion of securities that are valued using significant unobservable inputs.

a. Benefits

Allowing level 2 securities to be cross traded would enable registered funds to avoid the transaction costs they otherwise incur when accessing external markets.²⁰⁰ These avoided costs may include bid-ask spreads, dealer markups, and other execution expenses. More generally, in this discussion the term “transaction costs” includes both express costs (such as commissions, mark-ups, and mark-downs) and implicit costs, such as execution quality and market-impact effects.

The magnitude of these benefits would depend on how often registered funds with an affiliated adviser have complementary trading needs in level 2 securities and the extent to which

¹⁹⁹ See *supra* section II.A (Eligible Securities), discussing that observable inputs, including quoted prices, prices for similar securities, and other market-based inputs, are those already used in fund valuation under rule 2a-5, and that the proposal relies on existing valuation practices).

²⁰⁰ Some persons responding to the Staff Statement suggested that cross trades may also help advisers move securities that are difficult to obtain in the market to another fund that seeks exposure to them. See, e.g., SIFMA AMG Letter (“if fixed-income securities are sold externally, there is no assurance that those securities will be available to another fund seeking to buy them”); and T. Rowe Letter (“Cross trades can also benefit a buying fund wishing to acquire securities that are in very limited supply”).

fund complexes opt to engage in cross trading to meet those needs. Some complexes might realize only limited efficiencies if matched trading needs arise infrequently, while others with higher volumes of fixed-income trading could observe more substantial reductions in transaction costs.

In addition to transaction-cost savings, expanding eligibility to level 2 securities could also provide several ancillary economic benefits. As noted in section I.C, cross trades eliminate the need for a third-party counterparty, which may reduce exposure to counterparty risk. Section I.C also explains that internal cross trading can, in some circumstances, provide greater execution speed or certainty relative to open-market transactions, particularly when coordinating large trades or in periods of market stress. Further, section I.C describes that cross trading can provide an alternative source of liquidity for buying and selling funds when few broker-dealers maintain inventory in a particular security. Finally, as discussed in section III.B.3 of the baseline, fixed-income index funds and ETFs often face predictable rebalance-driven trading needs; enabling internal crosses of level 2 securities may reduce tracking error by allowing these funds to execute benchmark-related adjustments without incurring external market frictions, such as transactions costs or delays.

We estimate that the total annual monetized benefits of permitting cross trades under the amended framework are \$173 million (2026 dollars). This estimate reflects two components. First, for corporate-bond trades between two mutual funds, we use the SEC Staff White Paper data on the observed decline in quarterly cross trading following the implementation of

rule 2a-5.²⁰¹ Average quarterly volumes fell from approximately \$6.24 billion in the pre-rule period to about \$0.85 billion post-rule, a reduction of roughly \$5.39 billion. Applying post-rule transaction-cost spreads derived from the WRDS Bond Database to this decline yields an annual estimate of \$49.91 million in forgone savings, which we express in 2026 dollars using the GDP price index.²⁰² This represents the cost investors bear when trades that previously could be crossed are instead executed in the market. Second, for other fixed-income securities, we rely on an industry survey on cross trading, which documents the volume of cross trades by asset class—including U.S. Treasuries, mortgage-related securities, other asset-backed securities, international fixed income, bank loans, and commercial paper—almost all of which are level 2 instruments.²⁰³ Because we do not have data for the post-valuation-rule period, we assume the full reported cross-trade volumes would no longer occur. To estimate the resulting cost savings that funds currently realize, we apply the survey’s “normal-market-conditions” bid-ask spreads to each asset class. Summing the estimated annual savings across all categories results in an

²⁰¹ The SEC Staff White Paper analyzes cross-trading opportunities using Form N-PORT and Form N-CEN data for open-end mutual funds (excluding mutual funds with ETF share classes and money market funds that report on Form N-MFP) and does not include other registered funds (*e.g.*, ETFs or registered closed-end funds) or BDCs in its sample. Accordingly, the corporate-bond benefit estimate reflects only the mutual fund subset of registered funds.

²⁰² As a comparison, an academic study estimates that corporate-bond cross trading generated between \$64–\$96 million in annual transaction-cost savings. These annual figures are derived by multiplying the study’s quarterly estimates by four. The authors examine the entire 2008–2023 period because their empirical measures show that corporate-bond cross trading continued through and beyond the adoption of rule 2a-5. As they note, off-tape cross trading “declines dramatically” following the rule’s September 2022 effective date but “does not completely disappear,” and their holdings-based measure (MF Cross) even increases in certain post-rule subsamples. The academic estimates differ from the Commission’s \$49 million figure because the study measures total historical savings across the entire corporate-bond market, uses inferred crosses based on holdings and TRACE traded-pair data, and covers a multi-year period, while the Commission’s estimate reflects only the incremental forgone savings associated with the documented decline in registered-fund-to-registered-fund cross trades after rule 2a-5 and applies post-rule WRDS spreads to those observed reductions in activity. See Lina Han et al., *supra* note 182.

²⁰³ See ICI Letter.

aggregate benefit of \$173 million, expressed in 2026 dollars. These benefits represent recurring reductions in transaction costs that funds avoid by matching trades internally rather than routing them to dealers in the open market.

b. Costs

Funds relying on the expanded eligibility to cross trade level 2 securities would need to meet the rule's requirements, which would generate associated compliance and operational costs. These costs may include reviewing and documenting pricing-vendor methodologies, updating valuation and compliance procedures to incorporate observable-input pricing for cross trades, and establishing internal controls to oversee such transactions. For complexes without any cross-trading infrastructure for level 2 securities, these steps would represent one-time expenditures needed to ensure that cross trades of level 2 securities could be executed and monitored appropriately. In practice, however, establishing a cross-trading program for level 2 securities would also entail ongoing costs, including recurring reviews of pricing sources, periodic CCO and compliance oversight, and maintenance of trade-level and board-level records required under the proposed amendments. These recurring obligations reflect the continuing nature of pricing and oversight activities described in the proposal and therefore should be understood as ongoing, not solely upfront, costs. The size of these costs would vary depending on how closely a fund's existing systems align with the processes needed for cross trading level 2 securities. Registered funds that already obtain observable inputs for NAV purposes could in some cases rely on similar inputs to support cross-trade pricing, which would reduce, in some circumstances, the implementation costs associated with the cross trading of level 2 securities.

Currently, a decision to classify a security as level 2 or level 3 affects financial-statement disclosures and valuation oversight under rule 2a-5, but not whether the fund may enter into a transaction. Under the proposal, however, that classification would determine whether the security may be cross traded, which could, in some circumstances, influence how funds approach borderline classifications. Because determining whether observable inputs are sufficiently significant to support a level 2 classification can involve professional judgment under ASC 820, some funds might have a potential incentive to view certain borderline securities as level 2 when they wish to cross trade them. Any such incentive would likely be constrained by existing safeguards, including audit review of fair-value classifications, testing and board oversight under rule 2a-5, and quarterly CCO review of eligibility, and it is uncertain how these factors would interact in practice.

Cross trades in level 2 securities can involve normal valuation dispersion due to differences in observable inputs, NAV timing, or pricing-vendor methodologies. Although advisers may execute a cross trade only after determining *ex ante* that each participating fund is at least as well off as under reasonably available market alternatives, valuation discrepancies can produce *ex post* differences in realized outcomes across funds compared to what might have occurred if the transaction had been executed in external markets, particularly for less liquid assets. These differences can reflect modest distributional shifts in value between the participating funds,²⁰⁴ which arise from valuation dynamics rather than unequal treatment at

²⁰⁴ These offsetting price effects are commonly understood in economics as “transfers,” meaning that the distribution of value between the parties may differ depending on the execution price.

execution. The proposed conditions are designed to prevent trades at prices that are disadvantageous relative to the market, and to ensure the use of fair and consistently applied pricing methods for off-market trades.²⁰⁵

The conditions of the amendments—particularly the *ex-ante* best-interest determination, pricing requirements, and oversight provisions—are designed to contain the effects of such incentives and ensure that internal prices are applied consistently and without disadvantaging any fund. While underlying conflicts of interest exist regardless of the rule, expanding eligibility to level 2 securities increases the opportunity for advisers to act on such incentives because valuations for level 2 instruments rely on observable inputs that permit a wider range of plausible pricing outcomes than level 1 securities. In a principal–agent framework, this greater valuation discretion amplifies the potential for advisers to allocate internal prices in ways that advantage some funds at the expense of others. In addition, advisers may benefit reputationally when cross trades allow a fund or other client to avoid realizing losses that would have occurred had the position been liquidated in external markets, potentially improving reported performance. These incentives could, in the absence of effective controls, create risks that certain funds bear systematically less favorable pricing outcomes. The proposed conditions—including eligibility limits, pricing requirements, and oversight provisions—are intended to mitigate these risks, but to the extent they persist, they represent a potential cost of the proposed expansion. The amendments would also expand the set of transactions eligible for cross trading. As cross-trading

²⁰⁵ See, e.g., Bessembinder et al. (2006), documenting that estimated prices for corporate bonds in opaque OTC markets can diverge from actual market-clearing prices. Hendrik Bessembinder et al., *Market Transparency, Liquidity Externalities, and Institutional Trading Costs in Corporate Bonds*, 82 J. Fin. Econ. 251 (2006).

volume increases, aggregate exposure to the associated conflicts would rise even if the risk of any individual transaction remains unchanged.

This proposed amendment could also impose costs related to reduced availability of independent pricing information for certain securities. To the extent advisers internalize a greater share of transactions, fewer trades would be reported in public markets, diminishing the volume of observable inputs available for pricing level 2—and, to a lesser extent, level 1—securities. Over time, this reduction in market data could reduce the reliability of the pricing inputs used in both the NAV-based and current-market-price approaches for cross trades. In the extreme, a feedback effect could occur in which reduced public trading leads to less informative prices, which in turn increases uncertainty around subsequent cross-trade valuations. The costs of reduced observable pricing could also extend beyond the funds that engage in cross trading. Internal transactions do not generate the public trade data used by other market participants, including registered funds that do not cross trade, insurance companies, pension plans, index and benchmark providers, and pricing services that rely on executed transactions in comparable securities. These participants could bear some of the resulting reduction in pricing quality without receiving any of the transaction-cost savings associated with internalization. The magnitude of this effect would depend on the share of trading in an asset class that is internalized. As discussed in section III.C.6, the proposed reporting requirements would provide information on internalization by funds over time and by asset class.

2. Pricing of Cross Trades

Under the current rule, cross trades must be priced according to a prescriptive pricing method that varies by asset type, for example, last-sale prices for listed equities or the average of

the highest independent bid and lowest independent offer determined on the basis of reasonable inquiry for over-the-counter fixed-income securities. Historically, advisers generally satisfied the “reasonable inquiry” requirement for fixed-income cross trades by collecting multiple broker-dealer quotes. After the adoption of rule 2a-5, however, most fixed-income securities do not meet the definition of having readily available market quotations.

Under the proposed amendments, this prescriptive pricing requirement would be replaced with two pricing options: NAV pricing and current market pricing. If a fund elects to use current-market pricing, the adviser would also be required to periodically review whether the unaffiliated pricing sources continue to produce prices that reasonably represent current market conditions, and to maintain documentation of the pricing sources, their independence, and the results of those reviews. Because the revised framework permits advisers to draw from a broader range of pricing sources beyond broker-dealer quotes, the effects of this flexibility may be most significant for level 2 securities and for advisers with substantial fixed-income activity.

Both pricing options would be available regardless of the type of security being cross traded. In contrast to the current prescriptive hierarchy—under which many fixed-income cross trades historically relied almost exclusively on multiple broker-dealer quotes—the proposed pricing framework would allow a substantially wider range of pricing sources. Advisers could draw on evaluated prices, intraday vendor data, electronic-platform indications, and other observable inputs that reflect contemporaneous market conditions, rather than being limited to broker-dealer quotes, which for cross-trading purposes may have been accommodation quotes in practice — because the quoting dealer never intended to execute with the fund, dealers had no

incentive to provide actionable or accurate prices — and which could also be difficult to source and operationally burdensome for less-liquid fixed-income securities.

Because the proposal gives registered funds two alternative pricing methods, each fund would select the option it reasonably determines fits its valuation processes and operational needs. A fund's preferred pricing method may depend on considerations such as the markets in which the fund invests, the fund's trading strategy (including whether intraday execution is important), and the size and structure of the fund complex. Under either pricing method, advisers would retain flexibility to select the pricing source or valuation input they reasonably determine is appropriate for the security, and this flexibility may assist advisers in evaluating compliance with the rule's conditions because it allows them to rely on pricing sources and observable inputs that are already incorporated into their valuation workflows under rule 2a-5, reducing the operational frictions and data-collection steps that would arise if the rule required a single prescriptive source in all circumstances.

a. NAV Pricing

i. Benefits

Using NAV pricing could simplify operations when the fund's existing valuation process already produces a price for that day. A registered fund could rely on that value for cross trades rather than gathering broker-dealer quotes, thereby reducing operational steps. Because NAV pricing leverages processes that funds already use for valuation, advisers would be able to use the same infrastructure for cross-trade pricing, and improvements in those valuation processes could similarly extend to cross-trade pricing. These simplification benefits may be particularly relevant for level 2 securities, which constitute a large share of fixed-income fund portfolios and

are typically valued using observable inputs other than quoted prices in active markets for the particular security. For these securities, NAV pricing allows advisers to rely on established valuation workflows and pricing-service methodologies already subject to rule 2a-5 oversight, reducing the need to obtain real-time quotes for instruments that rarely trade intraday. NAV pricing would also provide certainty, familiarity, and transparency to fund investors regarding how cross trades will be valued. Because NAV pricing reflects the next-computed NAV rather than intraday price levels, NAV pricing could introduce timing-related differences when markets move between the execution time and the NAV strike; these differences are usually modest under normal market conditions but may be more pronounced during periods of elevated intraday volatility. When a fund uses the same pricing service for both NAV valuation and any intraday evaluated prices, we expect NAV-based and intraday evaluated prices to diverge only modestly, because both are derived from the same observable inputs and methodologies. The size of these benefits would vary across complexes primarily based on differences in the availability and timeliness of valuation inputs on the trade date, and—in the case of closed-end funds—whether a daily NAV is computed.

ii. Costs

Allowing registered funds to use the next-computed NAV to price a cross trade would impose minimal incremental costs for registered funds that already strike daily NAVs, because they can rely on their existing valuation processes. However, using the next-computed NAV introduces a potential timing-related economic cost: a fund executes the trade at one point in time but receives a price determined later, creating intraday price-risk exposure for both counterparties. In financial economics, this timing mismatch is analogous to execution risk—the

risk that market values move between the trade decision and the pricing timestamp. At the same time, some portfolio managers already execute market-on-close orders in ordinary trading, indicating that this type of timing-related risk is familiar and, in some circumstances, already managed within existing trading practices. Although the magnitude of this risk may be modest under normal market conditions, it may be more material during periods of elevated volatility and thus may represent a potential economic cost of NAV pricing under some circumstances. This timing risk is not symmetric across the two counterparties: if prices rise between trade execution and the NAV strike, the buying fund benefits at the expense of the selling fund, and if prices fall, the reverse is true; however, because subsequent price movements are unknowable at the moment the adviser places an NAV-priced cross trade, this asymmetry reflects an economic risk borne by both funds rather than a channel through which the adviser can intentionally time trades to favor one side. The proposed oversight conditions, including the CCO's quarterly and annual reviews, are intended to monitor whether any systematic patterns nonetheless arise. Because funds already record the price and supporting information for each cross trade under existing rule 17a-7, allowing funds to use the next-computed NAV would not introduce additional recordkeeping costs. And to the extent that broker-dealer quotes are non-actionable, uncompensated information requests, reducing reliance on such quotes is unlikely to impair broader broker-dealer relationships or execution quality for other transactions.

A fund that values a security at the bid price could, under NAV pricing, cross trade that security at the bid.²⁰⁶ If a cross trade occurs at the bid price, the selling fund would receive a

²⁰⁶ Under the current rule, cross trades must be priced at the average of the highest current independent bid and lowest current independent offer (a mid-market price), which prevents execution at a bid-only valuation.

price below a mid-market execution, with the difference accruing to the buying fund. Unlike the timing-related effects discussed above, which may favor either participant depending on subsequent price movements, any directional effect would arise only when both participating funds value the security at bid and therefore may use NAV pricing; if one fund values the security at mid and the other at bid, the cross trade could not be priced using NAV pricing under the proposal and current-market pricing would be required instead. The use of current market pricing may produce a price closer to mid and mitigate this concern. In addition, for a cross trade to occur under the proposal, the adviser must determine that it is in the best interest of each registered fund, which likewise may mitigate concerns about selling funds receiving prices below mid-market executions. We cannot estimate how many registered funds value securities at bid or the potential volume of affected trades. A selling fund may nevertheless benefit from avoiding market-impact costs, counterparty risk, liquidity risk, or other frictions associated with an open-market sale, which could offset some or all of the pricing difference in cases where both funds value at bid and the adviser determines that the NAV-priced trade is in each fund's best interest compared to reasonably available market alternatives.

NAV pricing could also give a fund's daily valuation of a security a transactional consequence it does not have today. Under the current framework, a stale or erroneous fair value affects a fund's reported NAV and the price at which its shares are issued and redeemed. Under NAV pricing, however, the same valuation would also determine the price of a cross trade with an eligible affiliate. If the valuation were later found to be incorrect, the fund would need to consider not only whether to correct its NAV under its existing error-correction policies, but also, depending on all the facts and circumstances, whether to reverse the trade or make the

affected fund whole. We cannot estimate how often such circumstances might arise. The valuation processes required by rule 2a-5, including periodic testing of fair-value methodologies, are intended to reduce this risk.

NAV pricing also assumes that both participating funds assign the same value to a security. Affiliated funds may, at times, reach different valuations because they use different pricing vendors or methodologies or compute NAV at different times of day. In such cases, the funds would not be able to use NAV pricing and would instead need to price the transaction at current market price or decline the trade if current-market pricing is not reasonably available. Funds may therefore incur costs to establish procedures for identifying and considering valuation differences when funds otherwise would use NAV pricing to price a cross trade, and some otherwise beneficial cross trades may not occur. We expect such differences to be uncommon within fund complexes that apply consistent valuation policies, but we lack data on their frequency or magnitude.

b. Current Market Pricing

i. Benefits

The current market pricing method would allow registered funds to rely on a broader and more modern set of pricing inputs than under the current rule's hierarchy. In addition to actionable broker-dealer quotes, advisers could use intraday evaluated prices from unaffiliated pricing vendors,²⁰⁷ and observable inputs made available through electronic trading platforms.

²⁰⁷ Unaffiliated pricing sources would include vendors or broker-dealers unaffiliated with the fund, its adviser, its promoter, or its principal underwriter. The adviser would retain flexibility to select a source it reasonably determines would represent current market value.

This flexibility is particularly relevant for level 2 securities, which often lack quoted prices but have robust observable inputs—such as yield curves, spreads, or comparable-bond data—that vendors incorporate into evaluated prices. Allowing advisers to use these sources may avoid the need to solicit broker-dealer quotes as was historically the case for certain fixed-income securities under rule 17a-7, prior to the adoption of rule 2a-5, and may provide more contemporaneous prices in markets where dealer quotes are sparse or delayed. This approach can provide a more contemporaneous price than the next NAV computation, particularly when market conditions change during the trading day. Access to intraday pricing allows advisers to execute cross trades at the same point in time that they make trading decisions for other portfolio transactions, giving them a price that reflects prevailing market conditions rather than end-of-day valuations. This alignment with normal trading workflows may be important for fixed-income and equity trading decisions that are made and executed intraday. Using an intraday price can modestly reduce the risk that market movements between trade decision and end-of-day NAV introduce unintended gains or losses to one side of the cross trade. In addition, certain intraday pricing sources may include contextual information—such as bid- and asked-price data—that can assist an adviser in determining, for purposes of the best-interest analysis, that executing at the obtained price does not disadvantage the fund or its affiliate relative to executing in the market.

The benefits of intraday pricing depend on unaffiliated sources providing sufficiently frequent and reliable updates. Some pricing services offer intraday evaluated prices, but we lack information on the asset classes covered, the frequency of updates, and the quality of these values relative to end-of-day prices. Where reliable intraday prices are unavailable, an adviser

seeking to execute a cross trade before the next NAV calculation may need to rely on other sources, such as broker-dealer quotes, which could limit expected operational savings. Advisers may also incur costs evaluating intraday-pricing products, which, unlike the end-of-day evaluated-price services used for NAV calculations, may not already be in established use.

Relative to the current baseline, in which advisers often must solicit multiple broker-dealer quotes to satisfy the pricing hierarchy for fixed-income cross trades, allowing advisers to rely on a wider range of current-market pricing sources—such as intraday evaluated prices and other observable inputs—may reduce operational costs and improve pricing accuracy by capturing more contemporaneous market information than periodically available quotes that the quoting broker-dealer knows will not be acted upon. This cost reduction would not stem from broker-dealer quotes being “expensive” but from reducing the staff time and operational effort required to solicit multiple quotes, particularly in less liquid fixed-income securities where dealers may be slow to respond. Although executable dealer quotes reflect actual tradeable levels, intraday evaluated prices and other observable inputs may provide a more up-to-date indication of prevailing market conditions when markets move between quote requests or when quotes are intermittent.

The periodic-review requirement would help ensure that prices derived from unaffiliated sources remain reliable over time, particularly in markets where liquidity and observable inputs fluctuate. By helping identify pricing that is stale, inconsistent, or outside the adviser’s established tolerance thresholds (such as deviations from expected ranges based on observable inputs) more quickly, this requirement may improve the accuracy and integrity of cross-trade pricing and reduce the risk that funds transact at off-market levels. Because advisers would also

need to document the pricing sources, their independence, and the results of these reviews, the requirement may further strengthen pricing discipline and transparency, albeit with some additional operational burden.

The magnitude of these benefits would depend on how frequently a registered fund trades securities whose market indications change throughout the day or whose evaluated pricing sources update frequently, as well as the degree to which the registered fund opts to use current market pricing in its cross trades.

The distribution of these benefits would vary across advisers and fund complexes. Advisers that trade frequently in fixed-income and other level 2 securities would generally experience the largest gains because they currently incur higher costs obtaining broker-dealer quotes under the existing hierarchy, and because observable inputs such as evaluated prices and spreads are more commonly available for these instruments than for less liquid securities, even when such inputs reflect prior-day or periodically updated data rather than continuous intraday changes. Large complexes with diverse fixed-income strategies also may benefit more from the expanded set of permissible pricing sources. By contrast, advisers primarily invested in level 1 securities, where quoted prices are readily available and updated continuously, may experience fewer incremental benefits from the current market pricing option.

ii. Costs

Although the increased flexibility may reduce operational costs associated with soliciting multiple broker-dealer quotes, some funds may still incur vendor fees if they need additional evaluated-price feeds to implement the method for certain securities. In instances where the adviser reasonably determines that broker-dealer quotes represent current market price, these

vendor-related costs could be avoided because the proposal would continue to permit their use. The adviser would also be required to periodically review whether the unaffiliated pricing sources produce reasonable results, which may entail staff time and analytical oversight. Because evaluated prices can differ across vendors or lag evolving market conditions, advisers might need additional monitoring to identify and address potential discrepancies. For level 2 securities, where evaluated prices may incorporate a range of observable inputs such as spreads, curves, and comparable-bond data, these discrepancies may arise more frequently, requiring advisers to perform additional periodic checks or cross-vendor comparisons to assess whether selected pricing sources remain reliable. Using an unaffiliated pricing source would not eliminate potential conflicts of interest. Pricing services may have incentives to accommodate clients on whose business they depend. Moreover, the adviser selects the pricing source, determines whether its price reasonably represents current market conditions, and may challenge or replace the obtained prices. Without effective controls, these functions could allow the adviser to influence the cross-trade price indirectly. The proposal's periodic review requirement and the CCO's review are intended to limit this risk, but any remaining ability to influence vendor-provided pricing would represent a potential cost of the method. Maintaining documentation of pricing sources, independence, and the results of periodic reviews would add to the operational workload. These costs could be partially mitigated because advisers already conduct certain vendor-pricing reviews for NAV valuation under rule 2a-5, and those processes may be leveraged for cross-trade pricing.

The proposed method would also give pricing services a more direct role in affiliated transactions. Today, an evaluated price is an input to a fund's fair-value determination and may

be tested or adjusted under its rule 2a-5 valuation procedures. Under the proposal, that evaluated price could determine the price of a cross trade. Because pricing-service usage is concentrated—the five most frequently reported providers each serve around 4,000 or more funds—the proposal could increase funds’ dependence on a small number of providers. This concentration could affect the terms on which services are offered and increase the consequences of service interruptions, pricing errors, or methodological weaknesses across multiple complexes. These effects may be mitigated because more than 5,000 funds obtain prices from at least four providers,²⁰⁸ and because the current-market-pricing option does not require use of pricing-service data, allowing advisers to rely instead on broker-dealer quotes or observable information from electronic trading platforms. We cannot estimate the magnitude of these potential impacts.

3. Transaction Costs and Fees

Under the current rule, cross trades must involve only cash payment against prompt delivery, and no brokerage commission or fee may be paid other than undefined “customary transfer fees.” This ambiguity has created uncertainty regarding whether operational charges, such as settlement fees, custody fees, or platform charges, are permissible and may have led to divergent practices among complexes. At the same time, because the determination of what qualifies as *de minimis* depends on a fund’s size and the context of the transaction, the proposal

²⁰⁸ These figures come from the baseline discussion of pricing-service usage in section III.B.3, which notes that the five most frequently reported pricing providers each serve around 4,000 or more funds and that over 5,000 funds obtain prices from at least four providers.

may allow some variation across complexes; however, these differences would reflect factual circumstances rather than interpretive uncertainty.

Under the proposed amendments, remuneration generally would be prohibited, except the proposal would permit *de minimis* payments to unaffiliated service providers (*i.e.*, not first- or second-tier affiliates) for clearing, settlement, custody, recording, or reporting the transaction. These payments would need to be small and operationally necessary for executing the transaction.

a. Benefits

By expressly allowing *de minimis* administrative payments to unaffiliated parties, the proposal could reduce operational steps by decreasing reliance on individualized interpretations of “customary transfer fees.” We do not anticipate that the proposal would materially increase or decrease the number or type of administrative fees charged, as these fees generally arise from ordinary settlement processes and the amendments are intended to clarify, rather than broaden, the range of permissible payments. Registered funds would spend less time reviewing routine settlement-related fees, although advisers would still need to exercise some judgment in confirming that a fee is *de minimis*. Reducing ambiguity around the “customary transfer fee” concept may also reduce compliance time spent evaluating whether a particular fee falls within that undefined category.

As discussed in section II.C, in some non-U.S. markets, funds are subject to mandatory settlement charges (such as stamp duties, transaction taxes, or local settlement fees). By allowing these existing charges to be treated as *de minimis* payments, the proposal may reduce a prior disincentive to engage in cross trades in certain non-U.S. markets where such fees are

unavoidable. The proposed *de minimis* allowance would simply clarify that such existing charges may be paid when they arise as part of ordinary settlement processes. Likewise, permitting *de minimis* fees charged by electronic trading platforms—limited to clearing, settlement, custody, recording, or reporting—may similarly reduce a practical barrier to cross trading on platforms that impose administrative fees, while clarifying treatment of administrative charges associated with platforms that already facilitate settlement workflows.

The extent of these benefits would depend on how often a registered fund encounters small administrative fees when settling cross trades. Complexes that currently absorb operational inefficiencies to avoid potential non-compliance could experience greater improvements, while complexes that already treat certain small fees as permissible might see more modest gains.

b. Costs

Under the proposal, the *de minimis* standard would apply on a per-trade basis. Although each payment is individually small, funds with higher volumes of cross trades may experience larger cumulative administrative outlays because the standard is applied to each transaction separately. These cumulative amounts would depend on a fund’s trading volume and the markets in which it trades, but they would not alter the per-trade nature of the *de minimis* condition.

Because funds already need to review settlement-related fees under the existing “customary transfer fee” standard, the proposal would not introduce a new type of monitoring obligation; rather, it would shift that existing review to a clearer, more bounded *de minimis* framework. Registered funds would need to monitor administrative fees to confirm they remain *de minimis* and relate only to clearing, settlement, custody, recording, or reporting of the transaction. We expect that monitoring under a *de minimis* standard would be no more

burdensome, and in many cases clearer, than evaluating whether a fee is “customary,” because the proposal limits permissible payments to specific administrative categories and ties the analysis to a fact-bounded, transaction-specific threshold rather than an open-ended industry-custom standard. Monitoring for compliance with the *de minimis* standard may require personnel of the fund or its service providers to review invoices or system reports and verify that each payment fits within the proposed categories, but we acknowledge that the applicable standards, the scope of permissible fees, and the associated analysis may differ from current practice—including in foreign markets where settlement structures, mandatory charges, or local transfer fees can vary—so some monitoring steps may not align perfectly with the existing customary-fee review. These activities are generally similar to the review already performed under the current rule, while reflecting the proposal’s clarified boundaries.

Funds or eligible affiliates that do not currently incur administrative fees when cross trading, because their existing cross trades occur in markets where such fees are not charged, would bear these costs to the extent they choose to begin making *de minimis* payments under the proposal. In practice, however, many registered funds already incur similar fees during settlement processes, especially in non-U.S. markets where stamp duties, settlement fees, and other mandatory charges are imposed as part of ordinary trade settlement, and the proposal would clarify that such existing fees may be paid in connection with a cross trade rather than introduce new fee types. Actual cost impact would vary based on a fund’s existing settlement arrangements and whether different settlement-related vendors or processes might be needed to handle clearing, settlement, custody, recording, or reporting.

Uncertainty may persist about what constitutes a *de minimis* fee across registered funds of different sizes. Larger registered funds may view a particular amount as *de minimis* relative to their trade sizes, whereas smaller registered funds could experience proportionally greater costs. Accordingly, the overall economic effect could vary across complexes.

Because the proposal would not define a specific amount or percentage as *de minimis*, funds would need to determine how the standard applies to particular fees. Some funds may incur costs documenting or obtaining legal advice about routine settlement charges that would not require separate analysis under a specified threshold. Others may avoid cross trades involving any fee to reduce the risk that the payment is later found inconsistent with the rule. In such cases, the cost would take the form of forgone cross trading benefits rather than additional expenses.

Determining whether a payment in a non-U.S. market relates to clearing, settlement, custody, recording, or reporting may require analysis of local law and market practice. Funds that cross trade non-U.S. securities may therefore incur costs obtaining advice from local counsel or service providers and updating that analysis as requirements change. These costs would be concentrated among complexes with substantial non-U.S. holdings and would generally arise for each relevant market rather than for each transaction.

The proposal would not specify which participant must bear a permitted payment. When both participants are funds, the allocation of that payment would determine how the cost is divided between two groups of shareholders, while the adviser making that decision acts for both funds. Although each payment would be small, consistently assigning fees to one participant could create recurring transfers between affiliated funds. Funds may therefore incur costs

developing and documenting an allocation methodology, and any unresolved discretion would add to the conflicts of interest discussed elsewhere in this section.

4. Best Interest Determination and Consistency with Fund Policies and Strategies

The current rule relies on board-approved procedures and quarterly board reviews to verify compliance with the rule's conditions, and these procedures do not require an evaluation of whether a particular cross trade is in the fund's best interest. Advisers already have existing fiduciary duties to act in the best interest of each client, including registered fund clients, but the current rule does not require a transaction-specific best-interest determination for each cross trade.²⁰⁹ Many advisers already consider whether a trade aligns with a fund's broader investment strategy, perform informal pre-trade checks or consider execution quality as part of their broader trading processes, but such practices vary across complexes and are not mandated by the rule.

Under the proposed amendments, an adviser would be required to determine that the cross trade would be in the best interest of the fund. In addition, as a condition of the rule, the transaction must be consistent with the fund's policies and investment strategies. Because this determination must reflect the particular characteristics of the fund and the security involved and the circumstances of the trade, advisers may need to tailor aspects of their analysis to the circumstances of each transaction, which may influence the associated economic effects.

a. Benefits

The proposal could encourage more deliberate pre-trade analysis by requiring that advisers compare the cross trade with reasonable execution alternatives, such as available market

²⁰⁹ See Standard of Conduct Release, *supra* note 7.

quotes, which may reduce the likelihood that a registered fund enters into a cross trade when trading in the market would yield more favorable terms. This more structured review also may improve advisers' ability to identify instances where trade-specific factors—such as liquidity conditions, anticipated execution quality, or signs of potential price impact—suggest that a cross trade is unlikely to provide a better outcome than external execution. In addition, by requiring advisers to make a documented, transaction-specific best-interest determination, the proposal may increase the *ex-ante* cost of improper practices such as cherry-picking, dumping, or parking, thereby discouraging such conduct.

Because of the express requirement that advisers evaluate best interest in connection with a cross trade, they may be more likely to identify instances where the proposed cross-trade price is not competitive with available external quotes.

For many advisers, the requirement would formalize review steps that are already part of existing trading practices, potentially resulting in more consistent documentation and more uniform application across trades. In complexes where pre-trade review practices are less developed or less consistently applied, the proposal could meaningfully strengthen the rigor and reliability of cross-trade decision-making. Tailoring the determination to the characteristics of the fund and the security may further enhance the accuracy of advisers' assessments, particularly in markets or asset classes where execution alternatives vary widely in quality. The extent of these benefits would vary depending on the robustness of an adviser's current pre-trade review processes. The costs section below discusses the transition and compliance burdens that may offset some of these gains.

b. Costs

Advisers would need additional time to make a best-interest determination for each cross trade and funds would need time to assess whether each cross trade is consistent with the fund's policies and investment strategies, although funds or advisers already performing similar analyses may experience smaller incremental costs. Costs may involve gathering information about external execution alternatives, such as indicative pricing, liquidity conditions, or available quotes, and comparing them to the proposed cross trade. Advisers also may incur incremental costs when tailoring their analysis to the specific characteristics of the fund or the security—for example, where market-based pricing inputs differ across asset classes or where the potential for market impact requires additional review. To the extent that portfolio management or trading personnel participate in these determinations, advisers may incur additional staff-time costs, including during periods when cross trades tend to occur in more concentrated windows. Advisers whose documentation is integrated into trading, order-management, or compliance systems also may incur one-time costs to modify those systems to capture the required elements of the determination. Supervisory review might also increase to ensure these determinations are completed and recorded consistently.

In situations where external pricing information is limited or changing rapidly, performing the best interest determination could lengthen the time required to reach a trading decision, creating variation in burdens across securities and complexes. Firms whose internal processes currently rely on more generalized or informal assessments may experience additional transition costs as they adapt workflows, including the allocation of review responsibilities among personnel. When both sides of a cross trade are registered funds, the proposal requires

separate best-interest determinations. Although the same personnel may conduct both reviews, each determination would need to reflect the circumstances of the specific fund. If the conclusions differ, the trade would not occur and the costs of making the determinations would not produce a completed transaction.

The proposed best-interest requirement also may need to be applied differently depending on a fund's trading methods and strategies. For example, advisers using fully automated or algorithmically implemented strategies may determine that they cannot perform the discretionary, transaction-specific review required under the best interest standard.

The proposed amendment would require advisers to prepare a transaction-specific record explaining why a cross trade is in the participating fund's best interest. Preparing this documentation imposes an incremental, per trade cost, and advisers may choose to avoid cross trades in situations where the expected savings relative to external execution are small. As a result, some cross trades that would have produced modest benefits under the expanded eligibility criteria may not occur. The Commission cannot estimate how often advisers might decline trades for this reason but recognizes that higher documentation costs could reduce the use of cross trading at the margin.

For cross trades in certain thinly traded level 2 fixed-income securities, the best-interest determination may partially offset the operational savings described in section III.C.2. That section identifies the elimination of the multi-dealer quote requirement as a potential benefit of the pricing provisions. However, because the best-interest determination requires the adviser to evaluate whether the proposed cross-trade price is reasonable relative to external execution alternatives, there may be circumstances in which the best interest requirement causes an adviser

to obtain additional market information—such as indicative dealer quotes or evaluated prices—beyond the information used to price the cross trade to support its best interest analysis. The extent to which this review would reintroduce quote-solicitation activity would depend on the adviser’s existing valuation infrastructure and the liquidity of the security involved.

5. Oversight Requirements

Under the current rule, oversight is board-centric: the board adopts and updates procedures and determines each quarter whether cross trades complied with them. The current rule does not place any specific related compliance responsibility on the fund’s CCO or anyone else. In practice, registered funds already have rule 38a-1 compliance programs that assign certain responsibilities to the CCO,²¹⁰ and the Commission staff has previously taken the position that a board may rely on a CCO representation that cross trades complied with the board-approved procedures,²¹¹ rather than performing transaction-level reviews of cross trades itself under rule 17a-7. Some registered funds also conduct post-trade testing or surveillance, but these practices differ significantly across complexes.

Under the proposed amendments, oversight would shift to a more structured, CCO-centered framework. The CCO would be required to conduct a quarterly compliance review of all cross trades and report the results to the board. In addition, the CCO would be

²¹⁰ Rule 38a-1 requires each registered fund to adopt and implement written compliance policies and procedures reasonably designed to prevent violations of the Federal securities laws, administer those policies through the fund’s CCO, and conduct an annual review of their adequacy and effectiveness. Rule 38a-1 provides flexibility for funds to tailor their compliance programs based on their facts and circumstances.

²¹¹ See IDC No-Action Letter (staff stating it would not recommend enforcement action if a fund’s board relies on a quarterly written representation from the CCO that rule 17a-7 transactions complied with board-approved procedures, rather than the board itself determining compliance).

required to perform an annual review designed to identify whether a registered fund may have been disadvantaged, an analysis that would include reviewing the timing and price of subsequent sales of securities purchased in cross trades, along with other information necessary to evaluate the trade. To facilitate this review, registered funds would need systems that can identify cross-traded securities and retrieve information about any subsequent sales of securities purchased in cross trades. The existing board-level quarterly determination would be replaced, and the board's role would pivot to reviewing the CCO's quarterly and annual reports.

a. Benefits

The proposed amendments may offer several oversight-related benefits. Shifting the oversight function to a structured, CCO-centered review within the fund's existing oversight framework under rule 38a-1, could reduce certain operational burdens. Regular quarterly checks and an annual look-back may help protect investors by enabling earlier detection of issues or unusual or anomalous patterns in cross-trading activity that could itself signal a potential concern, especially where such monitoring is not currently formalized. Board oversight could become more focused on broad themes, such as conflict risks or persistent pricing patterns, thereby enabling directors to identify systemic issues more effectively and avoid time-consuming, low-value transaction-level reviews.²¹² Enhanced systems that can identify cross-traded securities and retrieve information about subsequent sales would support more

²¹² See COSO (2013) noting that effective internal control systems can “eliminate ineffective, redundant, or inefficient controls” (p. 2), that “ongoing evaluations... provide timely information” to identify issues and emerging risks (p. 5), and that boards provide high-level oversight of internal control systems rather than performing operational-level reviews (pp. 2, 9). Committee of Sponsoring Organizations of the Treadway Commission (COSO), *Internal Control—Integrated Framework: Executive Summary* 1–20 (2013), available at https://www.coso.org/_files/ugd/3059fc_1df7d5dd38074006bce8fdf621a942cf.pdf.

effective annual reviews by the CCO and strengthen the fund's ability to detect whether it may have been disadvantaged. The scale of these benefits would depend on how frequently the registered fund engages in cross trading, the strength of existing surveillance tools, and how efficiently registered funds can automate tagging and reporting processes.

b. Costs

Registered funds would need systems capable of tagging and tracking each cross-traded security and producing analytics that compare cross-trade prices to subsequent market activity or other benchmarks. Depending on a fund's existing compliance and analytics infrastructure, the enhancements needed to support cross-trade reviews may overlap with systems already used for other regulatory or trading-quality assessments, such as execution-quality analytics or portfolio-level performance and pricing metrics. In such cases, advisers may be able to build on existing systems rather than develop entirely new ones, although some additional functionality may still be required to support the proposed cross trade-specific reviews. The CCO would need additional time to complete the required reviews, and registered funds would need to maintain documentation supporting those reviews, such as pricing determinations, and review outcomes, in addition to their existing recordkeeping obligations. At the same time, because the proposed amendments would eliminate the board's quarterly determination, registered funds may experience offsetting reductions in board-level oversight costs, reflecting lower demands on director time relative to the current rule. Further, assigning these reviews to a full-time CCO with direct or regular access to trade-level data may improve expertise matching and enhance the fund's ability to detect issues compared to periodic transaction-level checks by the board.

If additional CCO time or staffing is not available, these obligations could divert attention from other compliance responsibilities. Alternatively, adding compliance staff would increase costs to the fund and its investors or the fund's adviser. Concentrating these reviews in a single officer may also lead funds or advisers to adjust compensation, insurance coverage, or recruitment efforts for the CCO to reflect the increased scope of responsibilities.

The magnitude of these costs would vary based on the volume and complexity of a fund's cross-trading activity and how closely its existing compliance systems approximate what the proposed amendments would require. In addition, identifying which portion of a later disposition relates to securities acquired through cross trades may require tax-lot-level tracking or supplementary records, particularly where funds use average-cost accounting conventions that do not distinguish among different acquisition methods. For fixed-income securities held to maturity, the required systems may impose costs without generating a comparable disposition price, reducing the usefulness of the resulting data for the annual analysis. Differences between cross-trade prices and subsequent disposition prices may also reflect interim market movements rather than disadvantage, requiring the fund CCO to evaluate these distinctions as part of each review period. Further, because the disadvantage analysis occurs annually, any emerging pattern could persist for part of the year before detection, which may limit the effectiveness of this safeguard; this timing consideration is discussed more fully in section II.E. Additionally, shifting primary oversight responsibility from the board to the fund CCO may introduce governance-related costs. Under the proposal, only the fund CCO — not the adviser's CCO — would perform the quarterly and annual reviews and would prepare the required reports. Relative to other internal officers, fund CCOs have substantially fewer conflicts because they are subject

to rule 38a-1's independence framework: they are approved, compensated, and removable only by the board, and must report directly and separately to the board at least annually. These features mitigate conflicts relative to relying on adviser personnel. At the same time, some information asymmetry may remain where the fund CCO relies on adviser systems or has corporate reporting lines within the adviser or an affiliated entity, which may require additional documentation or verification. While boards would continue to review quarterly and annual CCO reports, the move from direct determinations to report-based oversight may lessen transparency into transaction-level details. However, this shift is consistent with the compliance structure established under rule 38a-1 and may reduce low-value operational burdens for boards by allowing them to focus on higher-level oversight.

6. Reporting

Under current requirements, some registered funds report on Form N-CEN whether they relied on certain statutory or rule-based exemptions (including rule 17a-7) during the reporting year. This disclosure is limited to a yes/no indicator and does not provide any information about the volume, type, or characteristics of a fund's cross trades. Funds' financial statements also include related-party disclosures under Regulation S-X, which may capture cross trades in aggregated form, but these disclosures vary across complexes, are not presented in a standardized or structured format, and are not tagged or readily comparable across funds. As a result, while some information about affiliated transactions is currently available, there is no consistent, publicly available reporting that provides structured metrics specifically describing cross-trading activity or its composition by asset class. Advisers track cross trades internally for

compliance and operational purposes, but these internal records are not reported in a uniform or machine-readable manner to the public or the Commission.

Under the proposed amendments, Form N-PORT and Form N-MFP filers that engaged in cross trades of portfolio investments in reliance on rule 17a-7 during the preceding twelve-month period would be required to report four data points for each asset type (or category of investment, in the case of Form N-MFP) in U.S. dollars. These data points are: (1) the aggregate value of portfolio investments the registered fund purchased under rule 17a-7, (2) the aggregate value of portfolio investments the registered fund purchased, (3) the aggregate value of portfolio investments the registered fund sold under rule 17a-7, and (4) the aggregate value of portfolio investments the registered fund sold. These data would be provided for the reporting period and would appear on the same filing and public availability schedule that applies to each form.

Some funds, such as BDCs, would not be subject to these standardized cross-trade reporting requirements. As a result, cross-trading activity in BDC portfolios would remain outside the scope of structured public reporting, limiting comparability between registered funds and BDCs and reducing the completeness of aggregate cross-trading information available to regulators and the public.

This approach would provide consistent, comparable information about the level and composition of cross-trading activity while avoiding trade-level reporting. It would give the Commission and the public, for the first time, standardized, machine-readable cross-trade metrics, improving transparency relative to the current regime of binary annual reporting and non-standardized financial statement footnotes.

a. Benefits

Standardized reporting would provide investors, regulators, and other market participants with insights into cross-trading activity across registered funds. Because funds do not currently disclose structured numerical information about their cross-trading activity, neither regulators nor the public can compare levels or patterns across funds today. The proposed structured monthly reporting, which includes four data points per asset type, would provide a more consistent, quantitative basis for such comparisons.²¹³ In addition, because the reporting framework includes total purchases and total sales by asset class, the new structured data may also improve the Commission's ability to monitor reporting funds' overall trading activity across asset classes and over time, including during periods of market stress. The practical value of such comparability may depend on how frequently a given registered fund engages in cross trading, and on whether existing Form N-PORT asset-type categories provide sufficient granularity to distinguish among the types of securities involved in cross trades. Because the extent and nature of cross-trading opportunities vary across asset classes, the magnitude of cross-trading activity reported by filers will naturally differ across funds with different portfolio compositions. This contextual information may help market participants better interpret differences in reported cross-trading levels across funds.

²¹³ Evidence from He et al., (2024) shows that when mutual fund disclosures are provided in a standardized, machine-readable structure, such as through the SEC's EDGAR system, investors use these disclosures extensively, and this engagement improves market-wide informational efficiency by enhancing price discovery and the accuracy of trading responses to earnings news. The study demonstrates that structured public disclosures do not only assist regulators but also generate broader market benefits by enabling investors to compare information across funds and incorporate it into trading decisions. Yichun He et al., *Are Fund Disclosure Views Informative to the Stock Market?* (Dec. 20, 2024), available at <https://ssrn.com/abstract=4940230>.

Beyond cross-fund comparability, the reporting requirement would facilitate comparisons of the amount of aggregate cross-trading activity occurring in a given asset class to the amount of trading activity in external markets for that asset class. This may allow both market participants and regulators to assess how the informativeness of public markets for an asset class changes as the share of the asset class traded internally via cross trades changes.

Standardized reporting on Form N-PORT and Form N-MFP could also improve the Commission's ability to monitor the use of cross trading over time. Because the reporting would provide consistent, structured, and machine-readable data across filers, it may facilitate analyses designed to identify trends in the aggregate volume of cross trades, the asset classes in which cross trading is most prevalent, and how cross-trading activity evolves as funds adjust to the proposed amendments.

Reporting could also support retrospective evaluations of whether increased internalization of trades has implications for measures of liquidity or the informativeness of public transaction data.²¹⁴ While the aggregate, monthly nature of the Form N-PORT and Form N-MFP reporting would not provide real-time transparency or price-discovery benefits, it may nonetheless allow researchers and regulators to study whether, and to what extent, cross-trading activity relates to changes in publicly observed trading patterns in certain asset classes. Any such benefits would be indirect and depend on how the data are used, but the availability of consistent aggregate information may lower the cost of conducting such analyses.

²¹⁴ We use the term “internalization” in its standard economic sense to refer to executing a transaction internally rather than through external trading venues, thereby avoiding bid–ask spreads, dealer markups, and market-impact costs.

Standardized public reporting may also modestly increase transparency around the extent to which funds use cross trading. Although any effect on investor behavior is likely limited given the lagged and aggregated nature of the disclosures, consistent public visibility into cross-trading volumes could provide some incremental disciplining effect at the margin. Market participants or examiners may take note of anomalous levels of reported cross-trading activity relative to peers, which may give advisers an additional incentive to avoid cross trading in situations where it is not in the best interest of investors. These effects are expected to be modest but may nonetheless contribute to greater public awareness of funds' cross-trading practices.

b. Costs

Registered funds would need to update reporting systems to capture and populate the new fields, assemble the data each month, and conduct internal verification prior to filing. Because funds are already required to maintain the underlying transaction-level information as part of their ordinary trading, accounting, and compliance processes—including data used for the CCO's required reviews—the incremental burden relates primarily to assembling and formatting existing data rather than generating new information, and may include modest increases in review effort to ensure the accuracy of the additional reported items.²¹⁵ The magnitude of these burdens will vary across funds depending on the extent of their cross-trading activity and the degree to which their existing systems already capture and organize the relevant data.

²¹⁵ See rule 31a-1(b)(1) and (b)(4) under the Investment Company Act (requiring funds to maintain detailed records of purchases and sales of securities and other trading-related records); and current rule 17a-7(g) (requiring funds to maintain written procedures and six-year records of each cross trade, including documentation used for compliance reviews).

In addition, the expansion of eligibility to level 2 securities may increase the number of cross trades executed by certain registered funds relative to the baseline. To the extent cross-trading volume increases, more funds would have cross-trade activity to report on Forms N-PORT and N-MFP, increasing the number of filers that must assemble and verify these values each month within their existing filings. The magnitude of any such increase would depend on each complex's trading activity, portfolio composition, and use of cross trading under the amended rule.

Because the two new data elements reporting a fund's total monthly gross purchases and total monthly gross sales by asset type would be publicly available under each form's existing filing and publication schedule, disclosure may impose costs beyond the direct costs associated with reporting holdings. These total gross purchase and sale aggregates—distinct from the rule 17a-7-specific purchase and sale amounts—could make the scale of trading activity within each asset type more visible, even in cases where end-of-month holdings show little net change, providing information that cannot be inferred solely from net month-end holdings.

For funds with highly concentrated strategies or exposure to very few asset types, monthly gross purchases and sales could provide incremental insight into repositioning or capacity constraints beyond what is already observable from quarterly holdings and public flow data. In such limited cases, market participants might be able to draw inferences that marginally affect the fund's future transaction costs. However, several features would help limit this risk: the data would be aggregated rather than transaction-specific, reported by asset type rather than security, and disclosed with a lag. We cannot estimate any remaining effect, which would

depend on portfolio concentration and the extent to which reported activity could be linked to particular positions and be subsequently exploited by other market participants.

The scale of one-time system changes may also vary across fund complexes. Some registered funds may need only minor adjustments to existing Form N-PORT processes, whereas others might require broader data-integration work to aggregate cross-trade values by asset type. Routine effort would also differ depending on the number of portfolios within a complex and the complexity of their holdings.

Reporting purchases and sales by asset type would require funds to map transactions from their portfolio-management, accounting, and compliance systems to the categories used on the applicable form. Because internal existing system categories may not align with the asset-type categories used on the form, funds would need to develop mapping conventions and determine how to treat transactions that do not resemble ordinary purchases or sales of portfolio securities.

7. Recordkeeping

Under the current rule, registered funds must permanently retain their cross-trading procedures and maintain six-year records of each cross trade and the materials used for board oversight. At the same time, existing requirements under rule 31a-1, rule 38a-1, and rule 2a-5 already obligate funds to maintain a broad set of transaction, compliance, and valuation-related records, including records in detail of all purchases and sales of securities, written policies and procedures, valuation materials, and documentation supporting oversight and testing. Because rule 38a-1 already requires retention of a fund's written policies and procedures, the permanent-retention requirement for cross-trading procedures in current rule 17a-7 is duplicative.

Conversely, the existing six-year recordkeeping requirement under rule 17a-7 does not capture all the types of materials that would be needed under the proposed oversight framework, such as documentation supporting annual pattern- or disposition-based testing.

Under the proposed amendments, the permanent-retention requirement would be removed, and procedural recordkeeping would be aligned with rule 38a-1. Registered funds would be required to maintain all information and materials used in the CCO's quarterly and annual reviews for a period of at least six years, such as any subsequent transaction data or other information needed to evaluate whether a registered fund may have been disadvantaged, although, for disposition-related analyses occurring many years after an original cross trade, the fund's permanent transaction records retained under rule 31a-1 and rule 31a-2 would supply the necessary data. Therefore, while the proposed amendments would require funds to retain cross-trade-specific oversight materials for six years, the long-term records needed for evaluating subsequent dispositions are already preserved under existing rules, and the proposal would not extend rule 17a-7 retention obligations beyond six years.

a. Benefits

In connection with the best-interest requirement described in III.C.4, the proposed recordkeeping amendments would help ensure that the adviser's determinations and the information used to support them are retained in a consistent and reviewable manner. This documentation would assist the adviser, the CCO, and the Commission in assessing whether cross trades complied with the rule's conditions. It would also support the proposal's oversight and testing requirements—specifically, the CCO's annual testing obligation to evaluate whether a registered fund may have been disadvantaged, which includes reviewing

subsequent-transaction prices and conducting pattern- or disposition-based analyses. Aligning the procedural retention requirement with that in rule 38a-1 would eliminate a duplicative retention obligation and simplify compliance administration. The extent of these efficiencies would vary. Complexes that already maintain detailed cross trade and pricing documentation might experience limited incremental benefit, while those with less comprehensive recordkeeping practices could see more meaningful reductions in review time.

By requiring funds to maintain more comprehensive materials supporting pricing, best-interest determinations, and quarterly and annual reviews, the proposed recordkeeping amendments may reduce one-off information requests in examinations and also facilitate remedial actions, such as reversing a trade or making a fund whole, as discussed in section II.E.3, where the retained records allow the adviser and CCO to identify and substantiate any disadvantage.

b. Costs

Registered funds would need to collect and retain all materials used in the CCO's quarterly and annual reviews, including pricing data, subsequent-transaction records, analytics, and any other information needed to determine whether a registered fund may have been disadvantaged. Retaining these materials for six years would increase storage needs, although the magnitude would depend on the volume of cross-trading activity and each fund's recordkeeping systems.

Uncertainty remains regarding how much additional work the annual review would require across complexes. Registered funds that already maintain disposition-price or

pattern-analysis files may face limited incremental burden, while those without such processes might need more time to build the necessary documentation and workflow infrastructure.

D. Aggregate Monetized Benefits and Costs

In this section, we quantify and present aggregate monetized benefits and costs across affected entities and over time. The monetized benefits include the estimated transaction-cost savings from cross trading corporate bonds and other level 2 fixed-income assets, based on cross-trade volumes and bid-ask spreads. These estimates do not include benefits from cross trading equity securities, because equity securities generally have readily available market quotations (level 1); any equity securities that are classified as level 2 are not separately quantified due to insufficient data. We also exclude benefits from cross trading municipal securities, because municipal cross trades have continued under existing staff no-action letters. Additional potential cost savings from cross trading other level 2 assets—including certain additional fixed-income instruments or loans—cannot be quantified with available data. As a result, the monetized cross-trading benefits reported in this section should be interpreted as a lower bound. We do not quantify any potential benefits associated with the new reporting requirements on Forms N-PART and N-MFP because we do not have data that would allow us to estimate the magnitude of these benefits—such as how standardized cross-trade reporting might affect investor decision-making, regulatory monitoring, or market liquidity.

We also quantify and include the monetized compliance costs associated with the proposed amendments to rule 17a-7, as well as the recurring internal and external costs associated with additional reporting requirements under Forms N-PART and N-MFP, as described in the PRA. These estimates assume that each affected entity realizes the full amount

of monetized benefits and costs shown; in practice, benefits and costs may vary depending on existing practices and how those practices change under the proposed amendments.

1. Aggregate Monetized Benefits and Costs Across Affected Entities

Tables 4 and 5 report the benefits and costs, respectively, that are monetized in this economic analysis, aggregated across all affected entities. To aggregate these monetized effects, we use estimates of the number of affected parties and burdens under the Paperwork Reduction Act in section IV. Because cross trading under rule 17a-7 is optional, the actual benefits and costs realized may differ from the aggregates presented here if some funds choose not to engage in cross trading.

We estimate that the total aggregate annual monetized benefit is \$173,018,571. The aggregate monetized benefit reflects estimated transaction-cost savings from cross trading between registered funds within the same fund family and their affiliates. As noted above, the estimate excludes potential benefits from cross trades in asset classes for which usable data are not available—including Level 2 equities, municipal securities that continue to be eligible under existing staff no-action letters, and other Level 2 instruments or loans. It also does not include any benefits that could arise from the new reporting requirements on Forms N-PORT and N-MFP. Moreover, the estimated transaction-cost savings do not include potential cost savings from cross trades involving BDCs. BDCs do not file on Form N-CEN or Form N-PORT, and therefore the available data do not permit estimating their cross-trading activity or the associated transaction-cost savings. Accordingly, the quantified estimates presented here reflect only those affected entities for which usable reporting data exist.

Because the monetized estimate captures only a subset of the potential benefits of the amended framework, the estimate likely understates the full range of benefits to investors and advisers.

**Table 4: Aggregate Monetized Benefits from Cross Trading
(2026 Dollars)**

Security	
U.S. Treasury	\$21,749,470
Corporate Bonds	\$89,766,548
Other Mortgage-Related Securities	\$4,251,630
Other Asset-Backed Securities	\$2,658,918
International Fixed income	\$43,640,933
Bank Loans	\$10,787,089
Commercial Paper or CDs	\$163,983
Total	\$173,018,571

Notes: Annual benefits represent estimated transaction-cost savings from cross trading. Savings are calculated as cross-trade dollar volume multiplied by the relevant bid-ask spread for trades between two registered funds, and cross-trade dollar volume multiplied by half the spread for trades in which only one side is a registered fund. For all asset classes except corporate-bond cross trades between two registered funds, annual cross-trade volumes come from the ICI cross-trading survey, which reports 2020 fixed-income cross-trade activity by asset class. The ICI survey assumes that these 2020 cross trades would not be available following the implementation of rule 2a-5, and therefore the full 2020 volumes are used in estimating annual savings. For corporate-bond trades in which both sides are mutual funds (excluding money market funds), annual savings are based on SEC calculations using observed declines in quarterly cross trading following rule 2a-5. Average quarterly volumes fell from approximately \$6.24 billion (2019 Q2–2022 Q3) to \$0.85 billion (2022 Q4–2024 Q2), a reduction of about \$5.39 billion. Post-rule quarterly transaction-cost spreads—derived from the WRDS Bond Database—are applied to this decline to estimate the annual savings had pre-rule cross-trading levels continued. All other estimates use normal-market spreads, excluding stressed market conditions (March and April 2020), from the ICI survey’s “normal year” methodology. If, instead of normal-market bid-ask spreads, we applied the ICI survey’s stressed-market spreads from March and April 2020 to the same cross-trade volumes, the resulting aggregate annual monetized benefit would exceed \$320 million (2026 dollars). This reflects the significantly wider spreads observed during those months, which magnify the transaction-cost savings associated with internal cross trading.

We estimate that the total aggregate initial monetized cost is \$15,867,600 and the total aggregate annual monetized cost is \$13,695,310.

**Table 5: Aggregate Monetized Costs
(2026 Dollars)**

	Initial Cost Per Affected Entity	Annual Cost Per Affected Entity	Estimated Number of	Aggregate Initial Cost (D)	Aggregate Annual Cost (E)

	(A)	(B)	Affected Entities (C)	[(A) x (C)]	[(B) x (C)]
Rule 17a-7: Internal time costs	\$22,668 ^a	\$5,667 ^b	700 ^c	\$15,867,600	\$3,966,900
Rule 17a-7: External cost	N/A	\$1,548 ^d	700	N/A	\$1,083,600
Form N-PORT: Internal time costs (software users)	N/A	\$462 ^e	4,726 ^h	N/A	\$2,183,412
Form N-PORT: Internal time costs (vendor users)	N/A	\$462 ^f	8,778 ^h	N/A	\$4,055,436
Form N-PORT: External cost (software users)	N/A	\$100 ^g	4,726 ^h	N/A	\$472,600
Form N-PORT: External cost (vendor users)	N/A	\$200 ^g	8,778 ^h	N/A	\$1,755,600
Internal time cost (Form N-MFP)	N/A	\$459 ⁱ	318 ^j	N/A	\$145,962
External annual cost (Form N-MFP)	N/A	\$100 ⁱ	318 ^j	N/A	\$31,800
Total				\$15,867,600	\$13,695,310

Notes:

- ^a The initial internal cost per affected fund (\$22,668) reflects the PRA-estimated 12 initial internal burden hours for the proposed amendments to rule 17a-7, monetized using the PRA's blended \$1,889 hourly wage rate. These hours correspond to initial implementation activities associated with the amended rule's oversight and recordkeeping provisions and are performed by financial managers, lawyers, and fund board members, consistent with the occupational mix underlying the blended rate.
- ^b The annual internal cost per affected fund (\$5,667) reflects the PRA-estimated 3 hours of ongoing annual internal burden for the proposed amendments to rule 17a-7, monetized at the PRA's blended \$1,889 hourly wage rate. The blended rate incorporates financial managers, lawyers, and fund board members, as described in the PRA wage-rate methodology.
- ^c The estimate of 700 registrants for rule 17a-7 is drawn from the PRA, which identifies 700 registered funds and BDCs expected to rely on the amended rule.
- ^d The external annual cost per fund of \$1,548 for rule 17a-7 is based on the PRA assumption of 2 hours of outside legal services at \$774 per hour.
- ^e For Form N-PORT filers using software (4,726 funds), the annual internal cost of \$462 per fund reflects 1 hour of internal burden at the \$462 wage rate, as described in the PRA table.
- ^f For Form N-PORT filers using third-party vendors (8,778 funds), the annual internal cost of \$462 per fund likewise reflects 1 hour of internal burden at the \$462 wage rate.
- ^g The external annual cost per software-using Form N-PORT filer (\$100) and per vendor-using filer (\$200) are drawn from the PRA estimates of increased external cost burdens for each filer type.
- ^h The estimated numbers of Form N-PORT filers — 4,726 software users and 8,778 vendor users — are based on PRA estimates that 35% and 65%, respectively, of the 13,504 total Form N-PORT filers fall into these categories.
- ⁱ The annual internal cost per Form N-MFP filer (\$459) reflects 1 hour of internal burden at the blended \$459 hourly wage rate described in the PRA, which incorporates financial managers, accountants/auditors, database administrators, and financial/investment analysts. The annual external cost per filer (\$100) is the

PRA-estimated increase in external service-provider costs associated with reporting cross-trade-related information.

j The estimate of 318 affected money market funds required to file Form N-MFP is based on March 2026 Form N-MFP filings, as reported in the PRA.

2. Present Values and Annualized Values of Aggregate Monetized Benefits and Costs

Consistent with the requirements of Executive Order 12866, the Commission reports estimated total monetized benefits and costs for all affected entities in two additional ways specified in OMB Circular A-4.²¹⁶ The two presentations are intended to address the fact that the various benefits and costs of the proposed amendments would not accrue at the same point in time; rather, benefits and costs that accrue sooner are generally more valuable than those that occur later in time.²¹⁷

We report (1) the present values of expected benefits and costs that are monetized aggregated across all affected entities, over a 10-year time horizon, starting in 2026, as well as (2) the annualized values over the same time horizon that are derived from the present values. This time horizon represents the period over which the principal benefits and costs that are monetized are expected to accrue.²¹⁸ The present values and annualized values account for the

²¹⁶ See E.O. No. 12866 (Sept. 30, 1993), 58 FR 51735, 51741 (Oct. 4, 1993) (requiring agencies to provide an analysis of benefits, costs, and regulatory alternatives to OIRA for significant regulatory actions); OMB, CIRCULAR A-4, at 31-34, 45 (Sept. 17, 2003) (providing guidance to agencies regarding compliance with E.O. 12866); *see also* E.O. No. 14215 (Feb. 18, 2025), 90 FR 10447, 10448 (Feb. 24, 2025) (requiring independent agencies to comply with E.O. No. 12866). In addition, E.O. 14192 requires agencies to provide their best approximation of the total costs or savings associated with each new regulation or repealed regulation consistent with the analyses required by E.O. 12866. *See* E.O. No. 14192 (Jan. 31, 2025), 90 FR 9065, 9066 (Feb. 6, 2025). For purposes of approximating the total cost savings and costs under E.O. 14192, the Commission uses the annualized monetized benefits and costs using a real discount rate of 7%. *See* Table 7 and accompanying discussion.

²¹⁷ *See* CIRCULAR A-4, at 32.

²¹⁸ *See id.* at 31 (stating that “[t]he ending point should be far enough in the future to encompass all the significant benefits and costs likely to result from the rule”). For the purposes of this analysis, we assume

timing of benefits and costs through discounting, which is a procedure that accounts for the time value of money.²¹⁹

Table 6 reports the present values of the aggregate monetized benefits and costs from Tables 4 and 5, combining initial and annual monetized benefits and costs. The analysis uses annual real discount rates of 3% and 7% over a 10-year time horizon, starting in 2026.²²⁰ We estimate that the present value of total monetized benefits is \$1,497,858,170 using a 3% discount rate and \$1,257,023,044 using a 7% discount rate. We estimate that the present value of total monetized costs is \$134,430,780 using a 3% discount rate and \$115,367,441 using a 7% discount rate.

**Table 6: Present Value of Aggregate Monetized Benefits and Costs
over 10 years from 2026 to 2035
(2026 Dollars)**

Estimated Effects^a	3% real discount rate	7% real discount rate
Benefits	\$1,497,858,170	\$1,257,023,044
Costs	\$134,430,780	\$115,367,441

Note:

^a For each discount rate, the present value calculations are based on the aggregate monetized annual benefit reported in Table 4 and the aggregate monetized annual costs reported in Table 5. The analysis assumes: (i) all monetized costs are recurring annual costs and no one-time monetized implementation costs are

the effective date of the rule, as well as the start year for the analysis's time horizon, is 2026. The analysis uses calendar years and accounts for the compliance periods included in the release (see note a in Table 6).

²¹⁹ See *id.* at 32 (“The Rationale for Discounting”) & 45 (“Treatment of Benefits and Costs over Time”); see also OIRA, REGULATORY IMPACT ANALYSIS: A PRIMER, at 11 (Aug. 15, 2011), available at https://www.reginfo.gov/public/jsp/Utilities/circular-a-4_regulatory-impact-analysis-a-primer.pdf (“To provide an accurate assessment of benefits and costs that occur at different points in time or over different time horizons, an agency should use discounting. Agencies should provide benefit and cost estimates using both 3% and 7% annual discount rates expressed as a present value as well as annualized.”); HARVEY S. ROSEN & TED GAYER, PUBLIC FINANCE 151 (8th ed. 2008) (defining present value as “the value today of a given amount of money to be paid or received in the future”).

²²⁰ This approach is consistent with OMB Circular A-4. See CIRCULAR A-4, at 31-34 (stating that, “[f]or regulatory analysis, [agencies] should provide estimates of net benefits using both 3 percent and 7 percent” discount rates and discussing why those rates are reasonable default rates). Also, we use a mid-year discount rate. See OMB, CIRCULAR A-94, at 21-22 (Oct. 19, 1992) (stating that, “When costs and benefits occur in a steady stream, applying mid-year discount factors is more appropriate.”).

incurred; (ii) the monetized benefit reflects a recurring annual benefit beginning in 2026; and (iii) monetized benefits and costs occur in a steady stream over the 10-year time horizon from 2026 through 2035. Consistent with Circular A-4, the calculations use mid-year discounting and apply real discount rates of 3% and 7% to convert the annual streams of monetized benefits and costs into present values.

Table 7 reports annualized aggregate monetized benefits and costs using real discount rates of 3% and 7% over a 10-year horizon.²²¹ The lump sum present values of aggregate monetized benefits and costs reported in Table 6 are converted in Table 7 into a constant stream of annualized benefits and costs over a 10-year time horizon, starting in 2026.²²² Annualized benefits and costs may differ from an aggregation of the recurring monetized annual benefits and costs discussed earlier in the Economic Analysis because they incorporate the timing of benefits and costs, through discounting, and combine one-time and recurring benefits and costs.²²³ Because the monetized benefits are assumed to be constant each year over the analysis horizon, the annualized monetized benefits equal the yearly benefit amount. Accordingly, annualized total monetized benefits are estimated to be \$173,018,571 per year using both the 3% and 7% discount rates. We estimate that annualized total monetized costs are \$15,528,187 per year using a 3% discount rate and \$15,879,351 per year using a 7% discount rate.

**Table 7: Annualized Aggregate Monetized Benefits and Costs
over 10 years from 2026 to 2035
(2026 Dollars)**

Estimated Effects^a	3% real discount rate	7% real discount rate
Benefits	\$173,018,571	\$173,018,571
Costs	\$15,528,187	\$15,879,351

Notes:

²²¹ This approach is consistent with the recommended treatment of benefits and costs over time in Circular A-4. *See id.* at 45 (“You should present annualized benefits and costs using real discount rates of 3 and 7 percent”).

²²² For each discount rate, the annualized monetized benefits (costs, respectively) in Table 4 represent the constant annual stream of benefits (costs, respectively) whose present value over the time horizon equates the corresponding present value in Table 6. *See* note a, Table 7 for additional calculation details.

²²³ The annualized benefits and costs present these values over the 10-year time horizon, starting in 2026.

^a For each discount rate, the annualized values are calculated by dividing the corresponding present values in Table 6 by the sum of discount factors over the time horizon. The discount factor in year t of the time horizon is equal to $1/(1 + \text{discount rate})^{(t-0.5)}$.

E. Efficiency, Competition, and Capital Formation

The Commission considers the potential effects of its rules on efficiency, competition, and capital formation. This section describes the mechanisms through which the amendments could influence these areas. Potential channels include changes in how registered funds execute transactions, advisers' internal resource allocation, changes in how information is incorporated into public prices, and shifts in investor portfolio allocations in response to changes in net returns.

1. Efficiency

The proposed amendments may facilitate operational efficiency in two respects. First, by permitting cross trades of level 2 securities, the proposed amendments would allow registered funds with offsetting trading needs to internalize transactions that would otherwise be executed through external trading venues. When a registered fund internalizes a transaction, it avoids certain trading-related frictions, including bid–ask spreads, markups, and market-impact costs.²²⁴ The extent of this efficiency would depend on how frequently registered funds have complementary trading needs in level 2 securities, where most of these frictions arise. Second,

²²⁴ See, e.g., Harris (2003), Chapters 13–14 (dealer spreads and markups) and Chapters 14 & 21 (market-impact costs as transaction costs). Harris identifies the bid–ask spread, dealer markups, and price-impact effects as the core frictions faced when executing in public markets, all of which internalization avoids. Harris's discussion of internalization, however, addresses broker-dealer internalization of customer order flow; the concept is cited here only for its description of trading frictions, not for its application to cross trades between advisory clients. Larry Harris, *Trading and Exchanges: Market Microstructure for Practitioners* (1st ed. 2003).

the proposed pricing conditions may reduce the operational steps required to price a cross trade. Under the current rule, cross trading in non-exchange-traded fixed-income securities—*i.e.*, securities that trade over-the-counter rather than on an exchange—historically required gathering multiple bids and offers from broker-dealers through reasonable inquiry, which is a process that some assert had become more difficult as dealer willingness to provide such quotes declined. Under the proposed rule, a fund using NAV pricing would determine the cross-trade price within its existing valuation process, which is already subject to rule 2a-5 governance, rather than conducting a separate pricing exercise. A fund using current market pricing that relies on the same pricing source for both cross-trade pricing and NAV computation may be able to leverage due-diligence processes already maintained for that vendor, potentially combining that review with existing rule 2a-5 oversight. For complexes whose valuation and pricing systems already support level 2 observable inputs, these pricing provisions may lower administrative demands on compliance and trading staff.

The proposed amendments would also introduce new compliance steps that do not exist under the current rule. These include a pre-trade best-interest determination by the adviser for each cross trade, a periodic reasonableness review of current-market prices by the adviser, a quarterly CCO compliance review covering all cross trades during the preceding quarter, and an annual CCO review that includes disposition-price analysis of securities purchased in cross trades. Each of these steps would require real resources (*e.g.*, personnel time, recordkeeping infrastructure, and, in some cases, systems development) that funds do not currently expend in connection with cross trading. The magnitude of these costs would depend on the frequency and volume of cross-trading activity, the per-trade cost of making and documenting the best-interest

determination, and the extent to which funds can integrate the new oversight steps into compliance processes already maintained under rule 38a-1 and rule 2a-5, as well as an adviser's obligations under the antifraud provisions of section 206 of the Advisers Act.

The amendments may promote allocative efficiency by reducing the transaction costs that registered funds incur when adjusting their portfolios to reflect intended risk and return profiles. Most fixed-income securities have been ineligible for cross trading since the September 2022 compliance date of rule 2a-5. As a result, registered funds seeking to rebalance or otherwise adjust their fixed-income holdings must execute those transactions through external trading venues, incurring transaction costs even where an affiliated fund would be interested in taking the other side of the trade. By permitting cross trades of level 2 securities, the amendments may allow portfolio managers to reduce these frictions and maintain allocations that more closely reflect each fund's intended investment objectives and strategies. The timing of any such gains would depend on whether a fund's existing valuation and pricing systems already support level 2 observable inputs. Funds that already maintain these capabilities may realize gains more quickly than funds that choose to update their systems to support observable inputs.

A countervailing consideration is that level 2 securities, unlike level 1 securities, do not have readily available market quotations and are instead valued using observable inputs, either directly or indirectly. To the extent that the cross-trade price for a level 2 security does not accurately reflect the security's value, the cross trade may not move the security to the fund that most values it at a fair market price, which could reduce rather than improve allocative outcomes. The proposed pricing conditions, best-interest determination requirement, and CCO

oversight provisions are designed to mitigate this risk, but their effectiveness in practice is uncertain and would depend on the quality and consistency of the pricing sources used.

Because the amended framework may make it easier for advisers to internalize certain offsetting transactions, some trades that would otherwise occur in public markets may instead be executed internally. To the extent this internalization occurs, and to the extent that market participants would otherwise have learned from the transaction, if conducted in the open market, due to information gleaned from the trading activity of the affiliated fund or the trade's counterparty (*e.g.*, a broker-dealer), the informational efficiency of prices could be reduced. In addition, reduced post-trade transparency in the market for level 2 securities such as corporate bonds due to such internalization may increase the transaction costs for trades that do continue to occur in public markets, which could result in less efficient investment allocations for investors.²²⁵

The proposed reporting requirements on Form N-PORT and Form N-MFP, which would require registered funds to disclose aggregate cross-trading volumes by asset class, may partially offset the reduction in publicly observable transaction-level information by providing market participants with data on the scale of cross-trading activity relative to total trading activity in each asset class. The extent of this offset is uncertain and would depend on whether aggregate volume data are sufficient to inform participants' assessments of liquidity and pricing in the

²²⁵ See, *e.g.*, Edwards et al. (2007), showing that the increase in post-trade transparency facilitated by the introduction of TRACE reporting of corporate bond trades decreases transaction costs for investors. Amy K. Edwards et al., *Corporate Bond Market Transaction Costs and Transparency*, 62 J. FIN. 1421-1451 (2007).

relevant markets. We discuss the cost implications of reduced observable pricing information in more detail in section III.C.1.b.

2. Competition

The amendments may affect competition among registered fund advisers and fund complexes through two mechanisms that operate in opposite directions. The first mechanism could lead to greater concentration of competitive advantage among larger fund complexes. Advisers with larger complexes and higher volumes of level 2 fixed-income trading are likely to have more frequent opportunities to internalize offsetting transactions and, therefore, more opportunities to realize the cost reductions the proposed amendments are designed to permit.²²⁶ If those cost reductions are reflected in execution quality or net returns to fund shareholders, they may attract additional investor flows, increasing assets under management and further expanding the set of internalization opportunities available to larger complexes.²²⁷ Larger fund complexes also may be able to leverage economies of scale in complying with the rule's oversight and reporting requirements relative to smaller fund complexes, adding to this competitive advantage. This feedback between cost savings, net returns, and asset growth is a recognized feature of the

²²⁶ See, e.g., Berk & Green (2004), explaining how fund size and investor flows can reinforce competitive advantages among larger fund complexes. Jonathan B Berk, & Richard C. Green, *Mutual Fund Flows and Performance in Rational Markets*, 112 J. POL. ECON. 1269 (2004).

²²⁷ Prior research finds that greater scale can lower the costs borne by fund investors. Tufano & Sevick (1997) show that structural factors consistent with scale efficiencies are associated with lower shareholder fees; Baumol et al. (1990) provide foundational evidence of economies of scale in mutual-fund operations; Latzko (1999) similarly notes scale economies in U.S. mutual-fund operations and advisory-fee setting; and Lopez Rago (2026) finds that fees fall after mergers, suggesting that increases in operational scale are associated with lower investor fees. William J. Baumol et al, *The Economics of Mutual Fund Markets: Competition Versus Regulation* (Kluwer Academic Publishers 1990); Peter Tufano, & Matthew Sevick, *Board Structure and Fee-Setting in the U.S. Mutual Fund Industry*, 46 J. FIN. ECON. 321 (1997). David A. Latzko, *Economies of Scale in Mutual Fund Administration*, 22 J. FIN. RES. 331 (1999); Ricardo Lopez Rago, *When Funds Merge: What Happens to Fees? Evidence from Acquiring Mutual Funds and ETFs*, SEC Staff White Paper (2026) available at <https://www.sec.gov/files/dera-wp-funds-mergers-2602.pdf>.

asset-management industry and could allow scale-advantaged registered fund advisers to deepen their competitive position relative to smaller advisers that have fewer cross-trading opportunities. To the extent this mechanism operates, it could contribute to greater concentration within the registered-fund industry or shift the competitive balance among fund complexes of different sizes. The magnitude of any such effects is uncertain, but the direction of the mechanism suggests that larger complexes may benefit more than smaller advisers from the amended framework. The magnitude of any such competitive effect is uncertain and would depend on how frequently advisers of different sizes are able to generate offsetting cross-trade opportunities, and on the extent to which cost reductions ultimately benefit investors in the form of higher net returns or indirectly benefit advisers by supporting higher AUM-based fee revenue through improved performance or reduced pressure to lower advisory fees.

The second mechanism runs in the opposite direction. Several features of the proposed amendments may reduce some frictions currently associated with implementing cross-trading programs. The proposed pricing conditions would replace the current reasonable-inquiry standard (which some assert has become increasingly difficult to satisfy as dealer willingness to provide quotes has declined)²²⁸ with two pricing methods that leverage existing valuation and vendor infrastructure. The proposed shift from board-level quarterly compliance determinations to CCO-conducted reviews would align cross-trading oversight with compliance infrastructure

²²⁸ Several noted that satisfying the current rule’s reasonable-inquiry requirement has become more difficult as dealers have grown less willing to provide quotes solely for purposes of internal cross trades. *See, e.g.*, MarketAxess Letter (dealers “increasingly unwilling to provide bids and offers when they believe such pricing is requested solely in support of an internal cross”); FIMSAC Recommendations (obtaining multiple bids and offers for fixed-income securities is “difficult to impossible in most circumstances”); SIFMA AMG Letter (reduced dealer willingness to quote has made existing pricing requirements “impractical”); Letter from BondCliQ (Apr. 19, 2021) (dealers reluctant to provide non-actionable quotes).

that funds already maintain under rule 38a-1. To the extent these changes enable advisers that previously found the compliance costs of cross trading prohibitive, including advisers with fewer resources or less developed internal systems, the resulting expansion in participation could increase competitive pressure on execution quality, pricing discipline, and governance practices across the industry. This pro-competitive effect would partially offset the scale-advantage mechanism described above.

The magnitude of any scale-advantage mechanism would depend on the distribution of cross-trading opportunities across fund complexes of different sizes, the extent to which cost reductions are reflected in net returns, and the degree to which those returns attract incremental investor flows. The magnitude of the pro-competitive mechanism would depend on whether the proposed pricing conditions and oversight framework meaningfully reduce the barriers to implementing a cross-trading program, and on the extent to which advisers that previously found those barriers prohibitive would in fact begin cross trading under the amended framework. Data on both of these questions are needed to assess each mechanism, and the Commission requests comment on both.

3. Capital Formation

The amendments may influence capital formation through several economic mechanisms, though these effects are uncertain and, to the extent they occur, are expected to arise only incrementally. Relative to the approximately \$47 trillion in total assets held by registered funds, the estimated \$173 million in annual transaction-cost savings represents a very small reduction in industrywide expenses. Using asset-weighted average expense ratios for registered funds, of

0.30% and 0.32%,²²⁹ aggregate annual expenses are roughly between \$140 billion to \$150 billion. The estimated savings therefore amount to about 0.1 percent of total annual expenses, or approximately one basis point. If internalizing trades reduces transaction costs for registered funds and advisers, and if some portion of those savings is reflected in higher net returns for fund investors, investors could experience higher after-fee performance. This could lead some households to adjust the allocation of their existing savings toward registered funds. Because reallocations among savings vehicles do not change the total supply of household savings, this channel alone would not be expected to alter the aggregate amount of capital available to issuers. Higher net returns could also, in principle, lead some households to increase the level of their saving. Empirical research generally finds that household saving responds only weakly to changes in investment returns;²³⁰ accordingly, even if the amendments modestly increase after-fee performance, the expected incremental effect on aggregate household saving — and thus on the supply of investable funds — is likely to be limited. To the extent any such response

²²⁹ SEC calculations based on data from the Investment Company Institute, *2026 Investment Company Fact Book and Data Tables* (<https://www.icifactbook.org/26-fb-data-tables.html>). The combined expense-ratio range is derived by weighting long-term mutual fund expense ratios and ETF expense ratios by their respective asset shares. Long-term mutual fund assets by investment objective are taken from Table 3 of the Fact Book data files (equity, hybrid, and bond mutual funds), and the corresponding asset-weighted mutual fund expense ratios are taken from Figure 6.1. The mutual-fund component is calculated as the ratio of (i) the sum, across each mutual fund category, of the category's assets multiplied by its expense ratio, to (ii) total long-term mutual fund assets. ETF assets by investment objective are taken from Table 11 of the Fact Book data files, and ETF expense ratios for index and actively managed ETFs are taken from Figure 6.5. Because ETF assets are not reported by both objective and strategy, the ETF portion is represented as a range. The lower bound is calculated by applying index-ETF expense ratios to total ETF assets, and the upper bound is calculated by applying active-ETF expense ratios to those same assets. In both cases, the ETF expense-ratio range is formed as the ratio of (i) the sum, across each ETF objective category, of ETF assets multiplied by the corresponding index- or active-ETF expense ratio, to (ii) total ETF assets.

²³⁰ See B. Douglas Bernheim, *Taxation and Saving*, in 3 *Handbook of Public Economics*, 1173 (Alan J. Auerbach & Martin Feldstein eds., 2002), reviewing evidence that household saving exhibits only weak or near-zero sensitivity to changes in after-tax returns.

does occur, additional saving could place downward pressure on the cost of capital for firms by increasing the supply of investable funds, although the magnitude of this effect is expected to be small.

Reallocations of household savings could also shift investment toward assets that finance productive activity. If investors move funds from deposits or other lower-yield securities into registered funds that invest in corporate bonds or equities, increased demand for those securities could place downward pressure on required yields at the margin, thereby potentially lowering issuers' borrowing costs. This mechanism would operate only if transaction-cost reductions are passed through to investors in the form of higher net returns and if those higher returns induce the reallocations described above. At the same time, as discussed in the subsection on efficiency above, increased internalization may reduce the amount of transaction-level information reflected in public prices, which could, in turn, reduce price informativeness and place upward pressure on required returns. The magnitude of each of these effects is uncertain and would depend on the factors described above. Because these channels operate through distinct mechanisms, we describe their effects qualitatively and separately.

F. Reasonable Alternatives

This section discusses reasonable alternatives to the proposed amendments, focusing on different approaches the Commission could have taken in designing the cross-trading conditions, pricing framework, and reporting requirements. For each alternative, we outline how the approach would operate and consider its potential economic effects.

1. Allowing Cross Trades in Any Security

As an alternative to the proposed rule permitting cross trades in securities with readily available market quotations or that are valued based on observable inputs, the Commission could have proposed allowing cross trades in any security without regard to the availability of market-based or observable pricing inputs. In this alternative, registered funds would have maximum flexibility to internalize trades, which would expand the set of transactions where registered funds could avoid external trading costs. To the extent that registered funds holding securities without observable inputs compute their NAVs on a daily basis, a valuation would already be computed as part of the fund's NAV process and could serve as the cross-trade price under this alternative.

Because this alternative would also permit cross trades in assets without observable inputs, its principal incremental effect would involve level 3 securities, where valuation uncertainty is greater, and transaction data are generally not observable regardless of execution venue. Permitting cross trades in these securities could therefore increase the risk of economically meaningful valuation dispersion across accounts. Valuation dispersion, for these purposes, refers to pricing differences large enough to shift value between participating accounts where valuations rely heavily on subjective, non-observable inputs, such differences may be more difficult to detect and resolve.²³¹ Compliance and monitoring processes could require

²³¹ Academic research on corporate bond OTC markets shows that when securities lack reliable observable pricing, execution prices can vary widely across investors due to search frictions, dealer bargaining power, and limited transparency (conditions that can produce economically meaningful valuation disparities). See Maureen O'Hara et al., *The Execution Quality of Corporate Bonds*, 130 J. FIN. ECON. 308–326 (2018); and Hendrik Bessembinder et al., *Capital Commitment and Illiquidity in Corporate Bonds*, 73 J. FIN. 1615–1661 (2018).

greater investment and verifying the fairness of prices in illiquid or bespoke assets without observable inputs could become more challenging. The wider discretion afforded under this alternative could heighten the importance of managing advisers' incentives around trade direction, given that pricing for many newly eligible securities is highly subjective. This alternative could have the greatest incremental effect on BDCs, which generally hold a higher concentration of level 3 assets than registered funds and therefore would experience a larger expansion of securities eligible for cross trading under this approach. Finally, the broader scope of permissible trades under this alternative would introduce additional complexity for fund oversight personnel and fund boards.

Considering the greater valuation subjectivity associated with level 3 securities, this alternative may also necessitate additional safeguards beyond those in the proposal. For example, the Commission could require trade-by-trade board (or board committee) approval for cross trades in such securities, or enhanced documentation, escalation, and post-trade review processes to verify pricing fairness. These additional measures would aim to mitigate the heightened risk of valuation dispersion and adviser conflicts that would accompany permitting cross trades in securities without observable inputs.

This alternative could also affect competitive conditions if advisers differ in their ability to support more complex valuation or monitoring processes, and changes in the availability of transaction information may influence broader informational efficiency in the markets.

2. Alternative Approaches to Pricing Cross Trades

As an alternative to the two-method pricing framework proposed in the amendments, the Commission could have proposed a fully prescriptive single-method pricing requirement or, in

contrast, a principles-based pricing regime that relies primarily on adviser discretion. At the most prescriptive end, the Commission could have proposed that all cross trades be valued using a single uniform method. For example, the Commission could have mandated use of the NAV price or for registered funds that do not compute NAV on a daily basis or for which a current NAV is not available at the time of execution, a price determined consistent with the procedures and methodologies used under rule 2a-5 for determining fair value (or, for securities with readily available market quotations, at current market value). A uniform pricing mandate would provide greater consistency in the required pricing approach across advisers and complexes and could reduce oversight and compliance burdens for registered funds already computing daily NAVs. It may also simplify monitoring for boards, examiners, and investors, given that all trades would rely on a single, standardized workflow. At the same time, however, a pricing regime limited to NAV or values determined consistently with a fund's NAV processes under rules 2a-4 and 2a-5 could constrain cross-trading activity for registered funds that rely on intraday information to make a best interest determination regarding whether an intraday cross trade is appropriate. For certain securities, advisers may conclude that the mandated method does not adequately reflect time-sensitive or security-specific information, and therefore may decide not to engage in cross trades even when such trades could otherwise be efficient.²³² A uniform pricing requirement may also have distributional effects if advisers with portfolios that align poorly with the mandated

²³² Academic evidence indicates that corporate bond pricing and execution mechanisms that perform well in some contexts can be less reliable in others, given heterogeneity in market structure and liquidity across instruments, trade sizes, and conditions. See Terrence Hendershott & Ananth Madhavan, *Click or Call? Auction versus Search in the Over-the-Counter Market*, 70 J. FIN. 419–447 (2015); see also Raphael Schestag et al., *Measuring Liquidity in Bond Markets*, REV. FIN. STUD. 1170–1219 (2016).

method, such as closed-end funds that do not calculate NAV daily, face operational adjustments or reduced pricing accuracy.

At the opposite end of the spectrum, the Commission could have proposed a principles-based pricing regime under which advisers set cross-trade prices according to board-approved valuation policies without any prescribed pricing method in the rule. For example, advisers could be permitted to select among intraday evaluated prices, executable dealer quotes, pricing-service feeds, or model-based estimates, or even adviser-originated prices, with the selection made based on the adviser's judgment of prevailing market conditions and the pricing information available at the time. The adviser would be required to document the basis for each pricing selection.

This could provide adaptability across market conditions and asset classes and allow advisers to incorporate the most relevant inputs available at the time of the trade. However, greater flexibility would likely require more robust controls and oversight to manage adviser discretion, particularly because, although advisers would still be subject to a best-interest obligation, the alternative would rely on adviser-performed pricing-reasonableness checks at the time of the trade rather than on periodic reasonableness reviews required under the proposed rule. Differences in advisers' valuation procedures and resources could also reduce comparability across registered funds and complicate investor assessments.

3. Trade-Level Reporting Alternatives for Cross Trades

As alternatives to the proposed reporting amendments, the Commission considered two distinct reporting frameworks for cross-trading activity: (1) public trade-level reporting of each cross trade, and (2) confidential trade-level reporting submitted only to the Commission.

Under the first alternative, the Commission could have required registered funds to provide anonymized trade-level reporting of each cross trade to a publicly available transaction-reporting mechanism, similar to the way corporate and municipal bond trades are currently reported to the TRACE and RTRS systems. Such a reporting system could capture and publish information such as the timing, price, and volume of each cross trade while shielding the identity of the fund complexes or accounts involved in the transaction. Public trade-level reporting would give investors and third-party analysts insight into the use of cross trades across registered funds. It would also provide additional pricing signals to the market that may enhance the informational efficiency of market prices for cross-traded securities and improve valuation models for those securities. Trade-level reporting would allow both market participants and regulators to monitor and evaluate the prices at which cross trades occur, providing a potential disciplining effect that might help ensure that registered funds and their advisers effect cross trades at prices that are most favorable under the circumstances for each fund to both sides of the transaction. In addition, if regulators were given private access to the identities of the counterparties involved in a cross trade along with the publicly available pricing information, it could improve monitoring of pricing quality and adherence to cross-trading conditions. However, generating trade-level submissions would require additional operational investment. Registered funds would need to implement systems capable of capturing, validating, and reconciling trade-level records on an ongoing basis. High-volume complexes could face higher recurring burdens, while smaller registered funds might experience relatively higher costs per

trade, potentially discouraging the use of cross trades altogether.²³³ These costs could be mitigated to the extent that the systems developed and maintained by funds to comply with the proposed rule’s recordkeeping requirements could be leveraged for trade-level reporting purposes. Finally, adopting a trade level reporting mechanism would also raise separate operational, design, and cost considerations not contemplated by the proposed reporting amendments. For example, while registered funds have existing infrastructure for reporting on Forms N-PORT and N-MFP, funds and their advisers are not currently connected to systems like TRACE and RTRS. As a result, there would be costs associated with creating such connections, including operational, legal, and technology costs and potential costs associated with engaging a third-party vendor.²³⁴

Under the second alternative, the Commission could have proposed requiring registered funds to provide detailed trade-level reports of each cross trade exclusively to the Commission on a confidential basis. This alternative could be structured either as a substitute for the proposed aggregate reporting or as a complement to it, in which case both requirements would apply simultaneously. Under this approach, regulators would retain access to rich trade-level data for oversight and analysis. Confidential trade-level reporting would provide regulators with granular supervisory data — including the timing, pricing, counterparty identity, and volume of individual cross trades — that aggregate monthly reporting does not supply. This additional detail could

²³³ See Hendrik Bessembinder et al., *supra* note 205, finding that transaction-level transparency enhances monitoring and market quality but imposes substantial data-processing and reporting burdens, especially for high-volume institutions. See also Maureen O’Hara, *High Frequency Market Microstructure*, 116 J. FIN. ECON. 257–270 (2015) explaining that granular trade data require intensive validation, sequencing, and reconciliation, increasing operational costs for reporting entities.

²³⁴ See, e.g., SIFMA AMG Letter, Dimensional Letter.

enhance the Commission’s ability to detect pricing anomalies, identify patterns of potential self-dealing, and assess compliance with the rule’s conditions at the transaction level. Confidential submission would also reduce reputational risk for registered funds engaging in unusually large or uncommon cross trades, because the transaction-level detail would not be publicly available.

The incremental costs of this alternative relative to the proposed aggregate reporting would stem primarily from the operational requirements of trade-level data capture and submission. Registered funds would need systems capable of generating, validating, and transmitting individual transaction records rather than monthly aggregates, and high-volume complexes would face recurring burdens proportional to their cross-trading activity. The submission mechanism itself would also require design and implementation investment beyond what the proposed reporting amendments contemplate, since the form is not currently structured for this type of transaction-level reporting. Finally, confidential trade-level reporting could expose funds to the risk that this data is inadvertently exposed to external parties. To the extent that confidential trade-level reporting were adopted in addition to the proposed aggregate public disclosure, these costs would be additional to the costs of the proposed amendments, rather than a substitute for them.

If adopted as a substitute for the proposed aggregate public reporting, confidential trade-level reporting would reduce public transparency.²³⁵ Investors, researchers, and third-party analysts would have limited insight into registered funds’ cross-trading practices, and the

²³⁵ See, e.g., Luigi Zingales, *The Future of Securities Regulation*, 47 J. ACCT. RSCH. 391–425 (2009) (arguing that public transparency improves market discipline and external monitoring, whereas confidential disclosure limits informational benefits to external users).

informational benefits of standardized reporting would be narrower. To the extent that public disclosure of cross-trading activity would also help improve price informativeness in public markets for securities that are cross traded, a less transparent option would forego such benefits.

G. Request for Comment

We seek comment on the economic analysis, including whether the analysis has: (1) identified all benefits and costs, including all effects on efficiency, competition, and capital formation; (2) given due consideration to each benefit and cost, including each effect on efficiency, competition, and capital formation; and (3) identified and considered reasonable alternatives to the proposed amendments. We request and encourage any interested person to submit comments regarding the proposed amendments, our analysis of the potential effects of the proposed rule, and other matters that may have an effect on the proposed rule. We request that commenters identify sources of data and information as well as provide data (with documentation) and information to assist us in analyzing the economic consequences of the proposed amendments. If available, we request that commenters provide examples to illustrate answers. In addition to our general request for comments on the economic analysis associated with the proposed amendments, we request specific comments on the following aspects of the proposal:

71. How do commenters expect the expanded scope of eligible level 2 securities to affect trading practices or operational processes? Please describe any anticipated changes under different market conditions.

72. How do funds anticipate using NAV pricing versus current-market pricing? Are there circumstances in which one approach may be more operationally feasible or cost-effective than the other?
73. What types of data sources or pricing inputs do funds expect to rely on when determining prices under the current-market-pricing option? If available, please describe any expected changes in costs or procedures associated with maintaining these sources.
74. To what extent might a change in the number of trades executed internally versus externally affect the availability of observable pricing information for level 1 and level 2 securities? If possible, please provide data or examples.
75. Are there particular asset classes or market segments where changes in public trade volume could have more noticeable effects on the reliability of pricing inputs used for valuation or risk management?
76. How do funds expect the proposed quarterly and annual review structure to affect ongoing compliance processes? Please describe anticipated resource needs or system changes.
77. What types of operational adjustments, if any, might be required to assemble and report the proposed cross-trade information on Form N-PORT and Form N-MFP? If available, please provide estimates of associated costs or time requirements.
78. Do commenters have data or examples that could assist in quantifying potential transaction-cost savings associated with cross trades of level 2 securities? If so, please describe the methodology used.

79. How might the proposed amendments influence trading efficiency, operational workflows, or fund-level resource allocation? Please describe any expected variation across fund size, strategy, or asset classes.

IV. PAPERWORK REDUCTION ACT

A. Introduction

Certain provisions of the proposed amendments contain “collection of information” requirements within the meaning of the Paperwork Reduction Act of 1995 (the “PRA”).²³⁶ We will submit the proposed collections of information to the Office of Management and Budget (“OMB”) for review in accordance with the PRA.²³⁷ The proposed amendments would change the current collection of information burdens of rule 17a-7, Form N-PORT, and Form N-MFP under the Investment Company Act.

The titles for the existing collections of information are “Rule 17a-7 – Exemption of Certain Purchase or Sale Transactions Between an Investment Company and Certain Affiliated Persons Thereof” (OMB control number 3235-0214), “Rule 30b1-9 and Form N-PORT” (OMB control number 3235-0730), and “Rule 30b1-7 (17 CFR 270.30b1-7) under the Investment Company Act of 1940, ‘Monthly report for money market funds’ and Form N-MFP, ‘Monthly schedule of portfolio holdings of money market funds’” (OMB control number 3235-0657). An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid OMB control number. Each requirement to record information constitutes a collection of information requirement under the PRA. These collections

²³⁶ 44 U.S.C. 3501–3521.

²³⁷ 44 U.S.C. 3507(d); 5 CFR 1320.11.

of information would provide information to the Commission. The Commission staff would also use the collection of information in its examination and oversight programs. We discuss below the collection of information burdens associated with the proposed amendments.²³⁸

B. Rule 17a-7

Rule 17a-7 provides an exemption from section 17(a) of the Investment Company Act for purchases and sales of securities between registered funds and eligible affiliates. The exemption is subject to conditions intended to reduce the likelihood of overreaching.

The current rule requires that the fund maintain and preserve permanently a written copy of the procedures adopted by the board. Under the rule, the board is required to determine, at least on a quarterly basis, that all affiliated transactions effected during the preceding quarter in reliance on the rule were made in compliance with these established procedures. The rule requires the fund to maintain written records of this board determination and each rule 17a-7 transaction for a period of not less than six years.²³⁹

We propose amendments to rule 17a-7 to, among other things, expand the securities eligible to be cross traded, modernize how cross trades are priced and overseen, and revise related recordkeeping requirements. The proposed rule would remove from rule 17a-7 the requirement to maintain and preserve permanently a written copy of the registered fund's cross-

²³⁸ As discussed in more detail above, we anticipate that the economic effects of this proposal would be deregulatory in nature. *See* section III.D, *supra*.

²³⁹ Current rule 17a-7(g) requires the written record of the affiliated transaction to include the following information: a description of the security purchased or sold, the identity of the person on the other side of the transaction, the terms of the purchase or sale transaction, and the information or materials upon which the board determined that the purchase or sale complied with the procedures set by the board.

trading procedures.²⁴⁰ Consistent with the current rule, registered funds would be required to maintain and preserve written records of cross trades for at least six years and include records on each cross trade. A fund also would be required to keep records of the information or materials the CCO used to determine whether cross trades were effected in compliance with the conditions of the proposed rule as part of its quarterly review and whether any such transaction, or pattern of transactions, may have disadvantaged the fund relative to eligible affiliates as part of its annual review. That would include information or materials related to other transactions or information necessary to evaluate those cross trades, including, as is consistent with the oversight requirement in the proposal, documentation showing that the CCO considered the timing and price of any subsequent sale of a security purchased in a cross trade. Further, the proposed amendments would require the fund to keep records of the CCO's report to the fund's board on the results of the required reviews, with one type of report required at least quarterly, and the other type of report required at least annually.

The respondents to these collections of information would be registered investment companies and business development companies that make cross trades in compliance with rule 17a-7. We estimate that there are 700 such registrants.²⁴¹ Compliance with rule 17a-7 is required to obtain or retain the ability to cross trade certain securities.

²⁴⁰ This change would remove duplication with the requirements of rule 38a-1, which requires registered funds to maintain a copy of their policies and procedures reasonably designed to prevent violation of the Federal securities laws that are in effect or were in effect at any time during the last five years. *See* rule 38a-1(d)(1).

²⁴¹ This estimate is based on the 674 registrants as of December 2020, before rule 2a-5 went into effect, that indicated on their Form N-CEN filings that at least one of their funds/series rely on rule 17a-7. We round this to 700 registrants to recognize that the estimate based on Form N-CEN may be under-inclusive (*e.g.*, it does not include BDCs that relied on rule 17a-7). In the most recent PRA submission for rule 17a-7, the Commission estimated that there are 446 registrants that relied on the current rule. We estimate that the

In the most recent PRA submission for rule 17a-7, the Commission estimated the annual aggregate burden to comply with the current collection of information requirements is 2,230 burden hours and an external cost burden estimate of \$1,659,120.

We are adjusting upwards the collection of information burden in connection with the proposed amendments to rule 17a-7. Table 8 below summarizes our initial and ongoing annual burden estimates associated with the proposed amendments. The figures reflect our estimates of burden hours and costs averaged across funds that are estimated to engage in cross trading, recognizing that a fund's burdens hours and costs will depend on the frequency at which the fund engages in cross trading. The following estimates of average burden hours and costs are made solely for purposes of the Paperwork Reduction Act.

Table 8. Rule 17a-7 PRA Estimates

	Initial internal burden hours	Internal annual burden hours ¹	Wage rate ²	Internal time costs	Annual external cost burden
PROPOSED AMENDMENTS TO RULE 17A-7					
Proposed amendments to rule 17a-7	12 hours	7 hours ³	x \$1,889	\$ 13,223	\$1,548 ⁴
Number of registrants		x 700		x 700	x 700
Total new annual burden of amendments		4,900 hours		\$9,256,100	\$1,083,600
Total Estimated Burdens, Including Proposed Amendments					
Current burden estimates		2,230 hours			\$1,659,120
Revised burden estimates		7,130 hours			\$ 2,742,720
Certain products and sums do not tie due to rounding.					
Notes:					

proposed amendments would result in approximately an additional 254 registrants relying on the rule, resulting in the total estimate of 700. This figure reflects the number of registrants that we estimate would rely on proposed rule 17a-7. The number of funds/series that may rely on the rule would differ.

1. Includes initial burden estimates annualized over a 3-year period.

2. The \$1,889 wage rate reflects current estimates of 0.60 of the hourly rate for a financial manager ($\$730 \times 0.6 = \438), 0.30 of the hourly rate for a lawyer ($\$774 \times 0.3 = \232) and 0.10 of the hourly rate for a fund board of directors (assuming an average of 9 directors per board) ($\$12,186 \times 0.1 = \$1,219$) in the securities industry. To estimate the \$12,186 hourly rate for a fund board of directors, Commission staff used an occupational hourly rate of \$1,354 for Chief Executives to estimate the hourly rate for a single director and assumed an average of 9 directors per board. To calculate the occupational hourly rates used in this release, the Commission uses the May 2025 occupational mean hourly wage data from the Occupational Employment and Wage Statistics (OEWS) program of the Bureau of Labor Statistics (BLS) for "Securities, Commodity Contracts, and Other Financial Investments and Related Activities" (NAICS 523). See *Occupational Employment and Wage Statistics*, U.S. Bureau of Labor Statistics, <https://www.bls.gov/oes/>; see also *Standard Occupational Classification*, U.S. Bureau of Labor Statistics, <https://bls.gov/soc/> (describing occupational classification system used by BLS); Exec. Off. of the President, Off. of Mgmt. & Budget, North American Industry Classification System (2022), available at https://www.census.gov/naics/reference_files_tools/2022_NAICS_Manual.pdf (describing the industry classification system used by BLS and other agencies). The mean hourly wage for each occupation is multiplied by an employment cost index (ECI) factor of 1.0227, calculated as one plus the percentage change in the seasonally adjusted ECI wages and salaries of private industry workers from the second quarter of 2025 (ECI=173.563), which contains the May 2025 OEWS reference period, to the first quarter of 2026 (ECI=177.498), which is the date of the most recently available ECI observations when the occupational hourly rates used in this release were calculated. See *Employment Cost Index*, U.S. Bureau of Labor Statistics, Seasonal Data 2001-Present, available at <https://www.bls.gov/eci/tables.htm>. The adjusted mean hourly wage is then multiplied by a nonwage cost adjustment factor of 5.734, which accounts for nonwage costs borne by employers, such as bonuses, benefits, and overhead. This factor is calculated as the average over 2016-2025 of the ratio of the Bureau of Economic Analysis's gross output for the NAICS 523 to total wages across all occupations for the NAICS 523 in the OEWS data. See *Gross Output by Industry*, U.S. Bureau of Economic Analysis, <https://www.bea.gov/data/industries/gross-output-by-industry>; *Occupational Employment and Wage Statistics*, U.S. Bureau of Labor Statistics, <https://www.bls.gov/oes/>. For example, the \$774 occupational hourly rate for lawyers is calculated as $\$131.91 \times 1.0227 \times 5.734$, or approximately \$774 (where \$131.91 is the May 2025 mean hourly wage for lawyers in NAICS 523). The final product is the occupational hourly rate. See *Generally Updated Methodology for Calculating Occupational Hourly Rates* (Dec. 19, 2025), available at <https://www.sec.gov/files/method-occupational-hourly-rates.pdf>.

3. Our proposed estimates reflect an increase in initial burden of 12 hours, annualized over a 3-year period, ($12 \text{ hours} / 3 = 4 \text{ hours}$), and an increase of ongoing annual burden of 3 hours.

4. The \$1,548 external cost burden is based on 2 hours of time spent on rule 17a-7 records and an estimated \$774 per hour cost for outside legal services.

C. Form N-PORT

Form N-PORT requires registered management investment companies (except for money market funds and small business investment companies) and ETFs that are organized as UITs to report portfolio holdings information in a structured, XML data language. The form is filed electronically using the Commission's electronic filing system, EDGAR. We propose to amend Form N-PORT to require certain registered funds to provide additional information about their cross trade-related purchase and sale activity.

The respondents to these collections of information would be management investment companies (other than money market funds and small business investment companies) and ETFs that are organized as unit investment trusts. We estimate that there are 13,504 such funds

required to file on Form N-PORT.²⁴² The proposed collections of information are mandatory for the identified types of funds. Certain information reported on the form is kept confidential.²⁴³

In the most recent PRA submission for Form N-PORT, the Commission estimated the annual aggregate compliance burden to comply with the current collection of information requirements in Form N-PORT is 2,000,834 burden hours and an external cost burden estimate of \$177,742,893.²⁴⁴

We estimate that registered funds prepare and file their reports on Form N-PORT either by: (1) licensing a software solution and preparing and filing the reports in house; or (2) retaining a service provider to provide data aggregation, validation, and/or filing services as part of the preparation and filing of reports on behalf of the fund. We estimate that 35% of funds subject to the Form N-PORT filing requirements license a software solution and file reports on Form N-PORT in house, and the remaining 65% retain a service provider to file reports on behalf of the fund.

²⁴² This estimate of the number of registered funds required to file on Form N-PORT is based on data from filings with the Commission as of Dec. 31, 2025.

²⁴³ See General Instruction F of Form N-PORT.

²⁴⁴ The most recent Form N-PORT PRA submission was approved in 2024 (OMB Control No. 3235-0730). In 2024, the Commission adopted amendments to Form N-PORT that require funds to file monthly reports within 30 days of month end and that provide for publication of monthly reports with additional delay. While these amendments have not gone into effect, the approved PRA estimates reflect those amendments. As a result, the current burden estimates reflect the burden hours and external costs associated with a requirement for registered funds to file monthly reports with the Commission within 30 days of month end. In connection with the 2024 amendments, the Commission did not estimate additional burdens associated with changing the publication frequency of Form N-PORT reports. In 2026, the Commission proposed changes that, among other things, would provide registered funds with additional time to file monthly Form N-PORT reports and restore a quarterly publication frequency. See Form N-PORT Reporting Release, *supra* note 116. As the proposed cross trading reporting requirements would follow the same timeframes as generally required for Form N-PORT, if we were to adopt the Form N-PORT proposal, we also expect that the proposed cross trading reporting items would be reported and made public at the amended timeframes.

We are adjusting upward the collection of information burden in connection with the proposed amendments to report cross-trade information. Table 9 below summarizes our annual burden estimates associated with the proposed amendments to Form N-PORT. The figures reflect our estimates of burden hours and costs averaged across all reporting funds, recognizing that a fund's burdens hours and costs will depend on whether the fund engages in cross trading. The following estimates of average burden hours and costs are made solely for purposes of the Paperwork Reduction Act.

Table 9. Form N-PORT PRA Estimates

	Internal annual burden hours		Wage rate ¹	Internal time costs	Annual external cost burden ²
PROPOSED AMENDMENTS TO FORM N-PORT					
Funds that license a software solution to prepare Form N-PORT	1 hour	x	\$462	\$462	\$100
Number of funds ³	x 4,726			x 4,726	x 4,726
Funds that retain the services of a third-party vendor to prepare Form N-PORT	1 hour	x	\$462	\$462	\$200
Number of funds ³	x 8,778			x 8,778	x 8,778
Total new annual burden of amendments	13,504 hours			\$6,238,848	\$2,228,200
Total Estimated Burdens, Including Proposed Amendments					
Current burden estimates	2,070,316 hours				\$177,742,893
Revised burden estimates	2,083,820 hours				\$179,971,093

Certain products and sums do not tie due to rounding.

Notes:

1. The \$462 wage rate reflects current estimates of the blended hourly rate for an accountant and auditor (\$330), paralegal and legal assistant (\$281), and attorney (\$774) in the securities industry. For additional information on the methodology used to calculate this rate, please see the explanation in Table 8, note 2.

2. Our proposed estimates reflect an increase of external cost of \$100 for funds that license a software solution to prepare Form N-PORT reports and an increase of external cost of \$200 for funds that retain the services of a third-party vendor to prepare Form N-PORT reports.

3. Based on Commission filings, we estimate that there are 13,504 funds that file reports on Form N-PORT. We estimate that 35% of these funds (or 4,726) would license a software solution to prepare Form N-PORT while 65% (or 8,778) would rely on a third-party

D. Form N-MFP

Form N-MFP requires every registered investment company that is regulated as a money market fund under rule 2a-7 to report portfolio holdings in a structured, XML data language. The form is filed electronically using the Commission's electronic filing system, EDGAR. We propose to amend Form N-MFP to require money market funds to provide additional information about their cross trade-related purchase and sale activity.

The respondents to these collections of information would be money market funds. We estimate that there are 318 such funds required to file on Form N-MFP.²⁴⁵ The proposed collections of information are mandatory for the identified types of funds.

In the most recent PRA submission for Form N-MFP, the Commission estimated the annual aggregate compliance burden to comply with the current collection of information requirements in Form N-MFP is 46,000 burden hours and an external cost burden estimate of \$2,881,428.²⁴⁶

We are adjusting upward the collection of information burden in connection with the proposed amendments to report cross trade-related information. Table 10 below summarizes our annual burden estimates associated with the proposed amendments to Form N-MFP. The figures reflect our estimates of burden hours and costs averaged across all reporting funds, recognizing

²⁴⁵ This estimate of the number of registered funds required to file on Form N-MFP is based on data from filings with the Commission for filings received through March 2026.

²⁴⁶ The most recent Form N-MFP PRA submission was approved in 2023 (OMB Control No. 3235- 0657).

that a fund's burdens hours and costs will depend on whether the fund engages in cross trading. The following estimates of average burden hours and costs are made solely for purposes of the Paperwork Reduction Act.

Table 10. Form N-MFP PRA Estimates

	Internal annual burden hours		Wage rate ¹	Internal time costs	Annual external cost burden ²
PROPOSED AMENDMENTS TO FORM N-MFP					
Reporting for Money Market Funds	1 hour	x	\$459	\$459	\$100
Estimated Number of Money Market Funds ³	x 318			x 318	x 318
Total new annual burden of amendments	318 hours			\$145,962	\$31,800
Total Estimated Burdens, Including Proposed Amendments					
Current burden estimates	46,000 hours				\$2,881,428
Revised burden estimates	46,318 hours				\$2,913,228

Certain products and sums do not tie due to rounding.

Notes:

1. This represents a blended hourly rate of \$459 for a Financial Manager (\$730 per hour), Accountant and Auditor (\$330 per hour), Database Administrator (\$375 per hour), and Financial and Investment Analyst (\$399 per hour). The blended hourly rate was calculated as $(\$730 + \$330 + \$375 + \$399) / 4 = \$459$, as rounded to the nearest whole dollar. For additional information on the methodology used to calculate this rate, please see the explanation in Table 8, note 2.
2. Our proposed estimates reflect an increase of external cost of \$100 to prepare Form N-MFP reports.
3. This estimate is based on Form N-MFP filings as of March 2026.

E. Request for Comment

We request comment on whether these estimates are reasonable. Pursuant to 44 U.S.C. 3506(c)(2)(B), the Commission solicits comments in order to: (1) evaluate whether the proposed collection of information is necessary for the proper performance of the functions of the Commission, including whether the information will have practical utility; (2) evaluate the

accuracy of the Commission's estimate of the burden of the proposed collection of information, including the validity of the methodology and assumptions used; (3) determine whether there are ways to enhance the quality, utility, and clarity of the information to be collected; and (4) determine whether there are ways to minimize the burden of the collection of information on those who are to respond, including through the use of appropriate automated, electronic, mechanical, or other technological collection techniques or other forms of information technology.

Persons wishing to submit comments on the collection of information requirements of the proposed amendments should direct them to the OMB Desk Officer for the Securities and Exchange Commission, MBX.OMB.OIRA.SEC_desk_officer@omb.eop.gov, and should send a copy to Vanessa A. Countryman, Secretary, Securities and Exchange Commission, using any of the methods in the ADDRESSES section, with reference to File No. S7-2026-36. OMB is required to make a decision concerning the collections of information between 30 and 60 days after publication of this release; therefore a comment to OMB is best assured of having its full effect if OMB receives it within 30 days after publication of this release. Requests for materials submitted to OMB by the Commission with regard to these collections of information should be in writing, refer to File No. S7-2026-36, and be submitted to the Securities and Exchange Commission, Office of FOIA Services, 100 F Street NE, Washington, DC 20549-2736.

V. INITIAL REGULATORY FLEXIBILITY ANALYSIS

The Commission has prepared the following Initial Regulatory Flexibility Analysis (“IRFA”) in accordance with section 3(a) of the Regulatory Flexibility Act (“RFA”).²⁴⁷ It relates to the proposed amendments to rule 17a-7, Form N-PORT, and Form N-MFP.

A. Reason for and Objectives of the Rule and Form Amendments

The Commission proposes to modernize and enhance rule 17a-7 primarily by expanding the types of securities that are eligible to be cross traded, updating the rule’s pricing conditions, and replacing the rule’s current board oversight requirements with a framework that is intended to allocate oversight responsibility in an effective manner and enhance investor protection. The amendments also include changes to the rule’s recordkeeping requirements and provisions regarding certain payments in connection with cross trades. In addition, the Commission proposes to amend Form N-PORT and Form N-MFP to require registered funds that engaged in cross trades in reliance on rule 17a-7 during the preceding twelve-month period to report aggregate information, by asset class (or category of investment, in the case of Form N-MFP), about the value of securities a registered fund bought or sold, as well as the value of securities bought or sold in cross trades, during the reporting period.²⁴⁸ The objectives of the amendments are to broaden registered funds’ abilities to engage in cross trades that are beneficial to funds and their shareholders (*e.g.*, by avoiding certain transaction costs) while enhancing investor protections around these activities through effective oversight and additional transparency. Each of these objectives is discussed in detail in section II above.

²⁴⁷ 5 U.S.C. 603(a).

²⁴⁸ See *supra* note 111 for differences between the forms.

B. Legal Basis

The Commission proposes the rule and form amendments contained in this document under the authority set forth in the Investment Company Act, particularly sections 6(c), 8, 17, 24, 30, 31, and 38 [15 U.S.C. 80a-1 *et seq.*].

C. Small Entities Subject to Rule and Form Amendments

For purposes of Commission rulemaking in connection with the Regulatory Flexibility Act, an investment company is a small entity if, together with other investment companies in the same group of related investment companies, it has net assets of \$50 million or less as of the end of its most recent fiscal year.²⁴⁹ Commission staff estimates that, as of December 31, 2025, there are approximately 62 registered funds that are small entities. This includes 20 registered open-end mutual funds (including 1 money market fund), 7 registered ETFs, 34 registered closed-end funds, and 1 UIT that are small entities. Additionally, as of the same date, there are approximately 5 BDCs that are small entities.

D. Projected Reporting, Recordkeeping, and Other Compliance Requirements

The proposed amendments include reporting, recordkeeping, and other compliance requirements that would apply to small entities that rely on rule 17a-7 to conduct cross trades. We lack reliable data to estimate how many of the registered funds and BDCs that are small entities would choose to engage in cross trades under the proposed amendments. Because rule 17a-7 is an exemptive rule, registered funds are not required to engage in cross-trading activity.

²⁴⁹ See 17 CFR 270.0-10(a). The Commission has a pending proposal addressing the definition under the Investment Company Act of small organization and small business for purposes of the Regulatory Flexibility Act. The Commission encourages commenters to review the proposal to determine whether it might affect their comments on this IRFA. See Small Entity Proposing Release, *supra* note 134.

As a result, we expect that a registered fund—including a small entity—would choose to conduct cross trades under the proposed amendments to the extent that the benefits of cross trading (*e.g.*, the avoided transaction costs) would justify the regulatory costs (*e.g.*, the reporting, recordkeeping, and other compliance costs). We recognize that, due to economies of scale, smaller funds may be less likely to rely on rule 17a-7 to engage in cross trading as a general matter. This is because smaller funds may be less likely to benefit from cross trading (for example, due to fewer trading opportunities with eligible affiliates relative to larger funds). Due to the potential for smaller benefits, small entities likewise may be less willing to experience regulatory costs to be able to cross trade.

1. Reporting

Under the proposed amendments to Form N-PORT and Form N-MFP, registered funds that report on the forms and that engaged in cross trades of portfolio investments in reliance on rule 17a-7 during the preceding twelve-month period would be required to report the aggregate value of portfolio investments purchased or sold during the reporting period, calculated on a gross basis, and by asset type (or category of investment, in the case of Form N-MFP). Such registered funds also would be required to report the aggregate value of portfolio investments purchased or sold in cross trades in reliance on rule 17a-7 during the reporting period, by asset type (or category of investment). This information would assist investors, the Commission, and its staff in understanding the volume and nature of cross-trading activity across the registered fund industry. Further, the transparency provided by the reporting may help mitigate the potential conflicts of cross trading.

This reporting requirement would impose burdens on all Form N-PORT and Form N-MFP reporting funds that engage in cross trading, including those that are small entities. The specifics of these burdens are discussed in the Economic Analysis and Paperwork Reduction Act sections above. These sections also discuss the professional skills associated with complying with these requirements. The costs of compliance with the forms' reporting requirements would vary based on whether a registered fund engages in cross trading and, if so, the scope of those activities (*e.g.*, whether occurring in a single asset class or across multiple asset classes). As discussed above, we expect that registered funds that are small entities are less likely to engage in cross trades than larger funds. However, to the extent that small entities engage in cross trades, the compliance costs of Form N-PORT and Form N-MFP reporting likely would not be meaningfully different for smaller versus larger funds.

2. Recordkeeping

Registered funds that conduct cross trades under rule 17a-7 currently are required to maintain certain records related to their cross trades. In addition to requiring maintenance of those records, the proposed amendments would amend the recordkeeping requirements to require registered funds to maintain records of the information or materials the CCO uses to make the required determinations in connection with its quarterly and annual reviews and the CCO's reports to the board. The proposed amendments are designed to show compliance with the proposed amendments to rule 17a-7, help establish that a cross trade was in the best interests of the registered fund (rather than giving special treatment to affiliated party), and provide important information about cross-trading activity to Commission staff in connection with examinations.

The proposed recordkeeping amendments would impose burdens on all funds, including those that are small entities. We discuss the specifics of these burdens in the Economic Analysis and Paperwork Reduction Act sections above. These sections also discuss the professional skills associated with complying with these requirements. Small entities that currently rely on rule 17a-7 would already have recordkeeping systems related to their cross trades, but small entities that would newly engage in cross trades under the proposed rule may not have recordkeeping systems related to cross trades. As a result, the burdens of the recordkeeping requirements may differ between small entities based on whether they previously engaged in cross trading under the rule. Further, while small entities would already have recordkeeping systems related to their cross trades, those systems may need to be updated to the extent that the proposed amendments require different records from current practice. We would expect larger funds or funds that are part of a large fund complex to incur higher costs related to the new recordkeeping requirements in absolute terms relative to a smaller fund or a fund that is part of a smaller fund complex. However, we would expect a smaller fund to find it more costly, per dollar managed, to comply with the proposed recordkeeping requirements because it would not be able to benefit from a larger fund complex's economies of scale.

3. Oversight Requirements

The proposed amendments would require the fund's CCO, rather than the fund's board, periodically to review the fund's cross trades, while still requiring oversight by the fund's board. Specifically, the proposed amendments would require a registered fund's CCO to conduct quarterly and annual reviews and to report the results of those reviews to the board. The quarterly review would involve a review of all cross trades during the period to determine their

compliance with the rule. The annual review would involve a review of cross trades during the period, and other transactions by the fund or information necessary to evaluate the cross trades (including timing and price of any subsequent sales of securities purchased in cross trades), to determine if cross trades may have disadvantaged the registered fund relative to the eligible affiliate. The proposed amendments would eliminate provisions in the current rule that place additional requirements on fund boards, including to make at least quarterly determinations that cross trades were done in compliance with the fund's procedures and to adopt cross-trade procedures. The proposed amendments are designed to better align oversight requirements to business responsibilities, reduce burden on fund boards, and remove duplication with rule 38a-1.

The proposed CCO review and board reporting amendments would impose burdens on all funds, including those that are small entities. We discuss the specifics of these burdens in the Economic Analysis and Paperwork Reduction Act sections above. These sections also discuss the professional skills associated with complying with these requirements. We anticipate that the burdens associated with the proposed CCO review and board reporting requirements would vary depending on the volume and scope of a fund's cross-trading activities. To the extent that registered funds that are small entities engage in smaller volumes of cross trades relative to larger funds, as we anticipate would generally be the case, the burdens of the CCO review and board reporting requirements for small entities should likewise be smaller.

E. Duplicative, Overlapping, or Conflicting Federal Rules

The Commission has not identified any Federal rules that duplicate, overlap, or conflict with the proposed amendments.

F. Significant Alternatives

The RFA directs the Commission to consider significant alternatives that would accomplish our stated objectives, while minimizing any significant economic impact on small entities. We considered the following alternatives for small entities in relation to the proposed requirements to enhance the benefits of the proposal for small entities: (1) establishing different requirements that take into account the resources available to small entities; (2) exempting small entities from all or part of the requirements; (3) clarifying, consolidating, or simplifying requirements under the proposed rule for small entities; and (4) using performance rather than design standards.

Although we are not proposing different requirements for small entities, including consolidated or simplified requirements specifically for small entities, some aspects of the proposal, such as the ability to use NAV pricing to price cross trades, may help reduce compliance costs for small entities. Many registered funds, including many that are small entities, already compute their NAVs on a daily basis and have existing processes around these valuations. Rather than requiring a separate process for determining the price of cross trades, the proposed rule would allow registered funds to leverage their existing valuation processes to price cross trades. We are not proposing to allow only small entities to use NAV pricing because we view it as a fair and appropriate way to price cross trades generally, regardless of fund size.

With respect to consolidated or simplified requirements, we considered simplifying the oversight framework in the proposed rule for small entities. For example, rather than requiring separate quarterly and annual reviews, we considered requiring small entity CCOs to review and report to the board at least annually whether cross trades conducted during the review period

complied with the rule and may have disadvantaged the fund relative to eligible affiliates. This annual review and report cadence would align with other review and reporting obligations for fund CCOs under rule 38a-1 and may reduce burdens on small entities by requiring less frequent reviews and reports to the fund's board. If small entities engage in cross trades infrequently and in small sizes, this annual review cadence may be effective at addressing conflict of interest and overreach concerns without undermining investor protection. However, the size of a registered fund does not necessarily dictate the frequency and volume of its cross trades. As a result, there is a risk that an annual review requirement would not be effective for all small entities, particularly those that engage in cross trading at some frequency. Thus, we propose the same oversight requirements for all registered funds, regardless of size, but request comment on whether the oversight requirements should be consolidated or simplified for small entities.

The conditions necessary to rely on proposed rule 17a-7, and the associated reporting and recordkeeping requirements, are designed to allow registered funds to engage in a broader range of cross trades where such trades are beneficial to fund shareholders, while preventing cross trades that involve overreaching or other investor protection concerns. We are not proposing to exempt small entities from some or all these requirements because the investor protection benefits should apply to investors in smaller funds as well as investors in larger funds. We considered exempting registered funds that are small entities from the proposed requirement to report aggregate cross trading on Form N-PORT and Form N-MFP. If small entities engage in cross trades infrequently and in small sizes, the value of the reported information would be less significant than for larger funds that cross trade more frequently and in larger amounts. At the same time, the size of a registered fund does not necessarily dictate the frequency and volume of

its cross trades. In addition, even though a small entity's cross-trading activity is likely small relative to the overall market, that does not mean the activity is insignificant to the fund itself. Because we propose to mitigate the costs of Form N-PORT and Form N-MFP reporting by requiring aggregate cross-trading information, and because a small entity may engage in levels of cross trades that are significant in the context of that particular fund, we propose to require small entities to report cross-trading information on Form N-PORT and Form N-MFP. However, we are requesting comment on whether small entities should be excluded from the proposed amendments to these forms.

With respect to the use of performance rather than design standards, the proposed rule includes a mix of performance and design standards. For instance, the proposed rule includes performance standards in the current market pricing provision and in the provisions regarding CCO reviews. These provisions identify the objectives that funds must achieve (*e.g.*, using a price that reasonably represents the current market price, and reviewing cross trades for compliance with the rule) without mandating the particular approach to achieving the objectives. The proposed rule also includes some design standards. For example, the proposed rule identifies the scope of securities that registered funds could cross trade under the rule. As discussed above, limiting the scope of securities under the rule is designed to prevent overreaching and ensure that there is independent pricing information about securities that registered funds are permitted to cross trade. We are not proposing to use solely performance standards in the proposed rule because cross trades involve conflicts of interest, and thus the conditions of the proposed rule must be specifically designed to protect investors from the overreaching that can result from such conflicts.

G. Request for Comment

The Commission requests comments regarding this IRFA. We request comments on the number of small entities that may be affected by our proposed amendments and whether the proposed amendments would have any effects not considered in this analysis. We request that commenters describe the nature of any effects on small entities subject to the rules and forms, and provide empirical data to support the nature and extent of such effects. We also request comment on the proposed compliance burdens and the effect these burdens would have on smaller entities.

VI. CONGRESSIONAL REVIEW ACT

For purposes of Subtitle E of the Small Business Regulatory Enforcement Fairness Act of 1996 (also known as the Congressional Review Act),²⁵⁰ the Commission must seek OMB's determination whether a final regulation constitutes a "major" rule. Under the Congressional Review Act, a rule is considered "major" where, if adopted, it results in or is likely to result in:

- An annual effect on the economy of \$100 million or more;
- A major increase in costs or prices for consumers or individual industries; or
- Significant adverse effects on competition, investment, or innovation.²⁵¹

To help inform OMB's determination as to whether any final rule that results from the proposal would be a "major rule," the Commission solicits comment and data on:

- The potential effect on the U.S. economy on an annual basis;

²⁵⁰ See 5 U.S.C. chapter 8.

²⁵¹ See 5 U.S.C. 804(2) (defining "major rule").

- Any potential increase in costs or prices for consumers or individual industries;
and
- Any potential effect on competition, investment, or innovation.

Commenters are requested to provide empirical data and other factual support for their views to the extent possible, to inform OMB’s determination regarding whether any final rule following this proposal is likely to be a “major rule” for the purposes of the Congressional Review Act.

VII. OTHER MATTERS

This action is an economically significant regulatory action under section 3(f)(1) of Executive Order 12866 and has been reviewed by OMB, consistent with Executive Order 14215. This action, if finalized as proposed, is expected to be an Executive Order 14192 deregulatory action.

STATUTORY AUTHORITY

The Commission proposes the amendments to rule 17a-7 under the authority set forth in the Investment Company Act, particularly sections 6(c), 17, 31, and 38 thereof [15 U.S.C. 80a-6(c), 80a-17, 80a-30, and 80a-37]. The Commission proposes amendments to Form N-PORT and Form N-MFP under the authority set forth in the Investment Company Act, particularly sections 8, 24, 30, and 38 thereof [15 U.S.C. 80a-8, 80a-24, 80a-29, and 80a-37].

List of Subjects

17 CFR Parts 270 and 274

Investment companies, Reporting and recordkeeping requirements, Securities.

Text of Rule and Form Amendments

For the reasons set out in the preamble, the Commission proposes to amend title 17, chapter II of the Code of Federal Regulations as follows:

PART 270 —RULES AND REGULATIONS, INVESTMENT COMPANY ACT OF 1940

1. The authority for part 270 continues to read, in part, as follows:

Authority: 15 U.S.C. 80a-1 *et seq.*, 80a-34(d), 80a-37, 80a-39, 1681w(a)(1), 6801-6809, 6825, and Pub. L. 111-203, sec. 939A, 124 Stat. 1376 (2010), unless otherwise noted.

* * * * *

2. Amend § 270.17a-7 by revising to read as follows:

§ 270.17a-7 Exemption of certain purchase or sale transactions between an investment company and certain affiliated persons thereof.

(a) *Exemption for certain cross trades.* If the conditions of paragraph (b) of this section are satisfied, a purchase or sale transaction between a fund and an eligible affiliate is exempt from section 17(a) of the Act.

(b) *Conditions.*

(1) The transaction is a purchase or sale of a security for which market quotations are readily available or that would be valued by the fund based on inputs that are observable, either directly or indirectly.

(2) The transaction is effected at the independent current market price of the security. For purposes of this paragraph, the “independent current market price” is:

(i) The value the fund ascribes to the security in its next computation of the fund’s current net asset value under section 2(a)(41) of the Act (15 U.S.C. 80a-2(a)(41)) and §§ 270.2a-4 and 270.2a-5 on the business day on which the transaction occurs; or

(ii) The price determined by the fund's investment adviser to reasonably represent the current market price for the security using one or more unaffiliated pricing sources, provided that the adviser periodically reviews the reasonableness of prices used under this paragraph (b)(2)(ii).

(3) The transaction involves no consideration, other than cash payment against prompt delivery of a security, and no remuneration is paid in connection with the transaction, other than *de minimis* payments to unaffiliated parties for services provided for clearing, settlement, custody, recording, or reporting of the transaction.

(4) The transaction is consistent with the fund's policies and investment strategies, as recited in its registration statement and reports filed under the Act.

(5) The fund's investment adviser determines prior to the transaction that it is in the best interest of the fund.

(6) The fund's board of directors satisfies the fund governance standards defined in § 270.0-1(a)(7).

(7) The fund's chief compliance officer:

(i) Reviews no less frequently than quarterly all transactions during the preceding quarter that were effected under this section to determine their compliance with this section;

(ii) Reviews no less frequently than annually transactions during the preceding period that were effected under this section, as well as other transactions by the fund or information necessary to evaluate transactions effected under this section (including the timing and price of a subsequent sale of a security purchased under this section), to determine whether any such transaction, or pattern of transactions, may have disadvantaged the fund relative to the eligible affiliate(s); and

(iii) Reports to the fund's board of directors no less frequently than quarterly on the results of the review under paragraph (b)(7)(i) of this section and no less frequently than annually on the results of the review under paragraph (b)(7)(ii) of this section.

(c) *Recordkeeping.* The fund must maintain and preserve for a period not less than six years from the end of the fiscal year in which any transactions effected under this section occurred, the first two years in an easily accessible place, a written record of:

(1) Each transaction, setting forth a description of the security purchased or sold, the identity of the eligible affiliate on the other side of the transaction, and the terms of the purchase or sale transaction;

(2) The information or materials upon which the determination described in paragraph (b)(7)(i) of this section was made, including information or materials used to determine that each condition under paragraph (b)(1) through (6) of this section was satisfied with respect to each transaction;

(3) The information or materials upon which the determination described in paragraph (b)(7)(ii) of this section was made, including information or materials related to other transactions or information reviewed under paragraph (b)(7)(ii) of this section; and

(4) The reports to the fund's board of directors provided under paragraph (b)(7)(iii) of this section.

(d) *Definitions.* For purposes of this section:

Eligible affiliate means, with respect to a fund:

(i) Another fund that is an affiliated person, or an affiliated person of an affiliated person, of such fund; and

(ii) A person that is an affiliated person, or an affiliated person of an affiliated person, of the fund solely by reason of having a common investment adviser, investment advisers that are affiliated persons of each other, common directors, and/or common officers.

Fund means a registered investment company, including any separate series thereof.

Unaffiliated means a person other than:

(i) An affiliated person or promoter of, or principal underwriter for, a fund; or

(ii) Any affiliated person of such person, promoter, or principal underwriter.

PART 274 —FORMS PRESCRIBED UNDER THE INVESTMENT COMPANY ACT OF 1940

3. The general authority citation for part 274 continues to read as follows:

Authority: 15 U.S.C. 77f, 77g, 77h, 77j, 77s, 78c(b), 78l, 78m, 78n, 78n-1, 78o(d), 80a-8, 80a-24, 80a-26, 80a-29, and sec. 939A, Pub. L. 111-203, 124 Stat. 1376, unless otherwise noted.

4. Amend Form N-PORT (referenced in § 274.150) by adding new Item B.12.

Note: Form N-PORT is attached as Appendix A to this document. Form N-PORT will not appear in the Code of Federal Regulations.

5. Amend Form N-MFP (referenced in § 274.201) by adding new Item A.23.

Note: Form N-MFP is attached as Appendix B to this document. Form N-MFP will not appear in the Code of Federal Regulations.

By the Commission.

Dated: October 9, 2026.

Vanessa A. Countryman,

Secretary.

Note: The following appendices will not appear in the Code of Federal Regulations.

Appendix A—Form N-PORT

FORM N-PORT

* * * * *

Item B.12. Cross-Trading Information. Has the Fund engaged in cross trades of portfolio investments in reliance on rule 17a-7 [17 CFR 270.17a-7] during the preceding twelve-month period? [Y/N] If yes, provide the following to the nearest cent in U.S. dollars for each asset type category specified in Item C.4.a. For purposes of this Item, aggregate value means the value of portfolio investments purchased or sold calculated on a gross basis, without netting any purchases and sales. Do not include portfolio investments that the Fund held until maturity in the aggregate value of portfolio investments the fund sold.

- a. The aggregate value of portfolio investments the Fund purchased under rule 17a-7 during the reporting period;
- b. The aggregate value of portfolio investments the Fund purchased during the reporting period;
- c. The aggregate value of portfolio investments the Fund sold under rule 17a-7 during the reporting period; and
- d. The aggregate value of portfolio investments the Fund sold during the reporting period.

* * * * *

Appendix B—Form N-MFP

FORM N-MFP

* * * * *

Item A.23. Cross-Trading Information. Has the fund engaged in cross trades of portfolio securities in reliance on rule 17a-7 [17 CFR 270.17a-7] during the preceding twelve-month period?

☐ Yes ☐ No

If Yes, answer Item A.23.a through d. Provide the following to the nearest cent in U.S. dollars for each category of investment as specified in Item C.6. For purposes of this Item, aggregate value means the value of portfolio securities purchased or sold calculated on a gross basis, without netting any purchases and sales. Do not include portfolio securities that the fund held until maturity in the aggregate value of portfolio securities the fund sold.

- a. The aggregate value of portfolio securities the fund purchased under rule 17a-7 during the reporting period:
- b. The aggregate value of portfolio securities the fund purchased during the reporting period:
- c. The aggregate value of portfolio securities the fund sold under rule 17a-7 during the reporting period:
- d. The aggregate value of portfolio securities the fund sold during the reporting period:

* * * * *