

# SEC adopts rules and forms to modernize reporting requirements for registered investment companies

Stephen Cohen, Megan Johnson, Gary Brooks and Brooke Higgs

## Abstract

**Purpose** – To explain the new rules, forms, and amendments to current rules and forms (Final Rule) that the Securities and Exchange Commission (SEC) has adopted to modernize the reporting of information provided by registered investment companies (funds) and to improve the quality and type of information that funds provide to the SEC and investors.

**Design/methodology/approach** – Discusses the background leading up to the Final Rule, provides an overview and summary of the Final Rule's key components, and highlights issues that may be raised by the new reporting regime.

**Findings** – The Final Rule will have a significant effect on many funds. Funds will experience a substantially increased reporting burden with respect to both the frequency of reporting and the granularity of information required.

**Practical implications** – Fund managers and fund service providers should begin to evaluate the impact of the Final Rule, the processes that will need to be implemented to prepare filings on new forms, and the changes in fund disclosure practices that will be required in response to the amendments to certain forms.

**Originality/value** – Practical guidance from financial services lawyers specializing in the investment management industry.

**Keywords** U.S. Securities and Exchange Commission (SEC), Form N-CEN, Form N-PORT, Investment companies, Regulation S-X, Modernized reporting

**Paper type** Technical paper

Stephen Cohen ([stephen.cohen@dechert.com](mailto:stephen.cohen@dechert.com)) is a partner, Megan Johnson ([megan.johnson@dechert.com](mailto:megan.johnson@dechert.com)) is a partner, Gary Brooks ([gary.brooks@dechert.com](mailto:gary.brooks@dechert.com)) is an associate, and Brooke Higgs ([brooke.higgs@dechert.com](mailto:brooke.higgs@dechert.com)) is an associate in the Washington, DC office of Dechert LLP.

**O**n October 13, 2016, the U.S. Securities and Exchange Commission (SEC or Commission) adopted, by a 2-to-1 vote, new rules and forms, as well as amendments to certain rules and forms (Final Rule), to modernize the reporting of information by registered investment companies (funds)[1]. Guided by the recent implementation of enhanced data reporting requirements for money market funds and private funds, the Final Rule is designed to improve the quality and type of information that all funds provide to the SEC and investors. Among other things, the Final Rule requires that portfolio-wide and position-level information and census information be provided in a “structured data format”, which will allow the SEC to more efficiently analyze the data to respond to market and fund-specific events. SEC Chair Mary Jo White stated at the open meeting at which the Final Rule was adopted that the Final Rule

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represents a “sweeping change for the industry by requiring strong transparency provisions and enhanced investor protections”.

The Final Rule has four key components:

- Adoption of Form N-PORT, for reporting portfolio-wide and position-level information, and the rescission of Form N-Q.
- Adoption of Form N-CEN, for reporting census-type information, and the rescission of Form N-SAR.
- Amendments to Regulation S-X to require (among other changes) standardized reporting of derivatives holdings in a fund’s financial statements.
- Amendments to Forms N-1A, N-3 and N-CSR to require certain disclosures regarding a fund’s securities lending activities.

This article briefly discusses the background leading up to the Final Rule, provides an overview of the Final Rule and then summarizes its key components, highlighting various issues that may be raised by the new reporting regime. As further discussed below, the SEC decided not to take action with respect to proposed Rule 30e-3, which, as proposed, would have allowed a fund to satisfy current shareholder report delivery obligations by making the reports and certain other materials accessible on a fund’s website. The SEC continues to evaluate proposed Rule 30e-3, and Chair White stated that she has directed the staff to prepare a recommendation for the Commission’s consideration by the end of the year.

## Background

In fulfilling its role as the primary regulator of the asset management industry, the SEC relies on information included in reports and other filings made by funds, in order to: monitor funds and detect risks; inform policy- and rulemaking-related determinations; and help facilitate the Commission’s examination and enforcement activities. Over time, the fund industry has grown, developing new fund products and investment techniques that have increased the volume and complexity of information that funds disclose in their filings, which has made it more difficult for the SEC to efficiently utilize such information in fulfilling its regulatory function. At the same time, advances in technology have helped improve the ability to collect and analyze key information. The SEC has previously taken action to implement the reporting of information in structured data formats to help better analyze data<sup>[2]</sup>; this is designed to not only assist the SEC in fulfilling its regulatory function, but also to help investors and other fund industry participants evaluate reported information.

On May 20, 2015, the SEC issued its proposing release to modernize the reporting of information by funds (Proposed Rule)<sup>[3]</sup>. The SEC received 1,003 comments on the Proposed Rule, which informed certain modifications to the Final Rule. The Final Rule implements each of the key components of the Proposed Rule, with the exception of proposed new Rule 30e-3. The SEC adopted the Final Rule on October 13, 2016.

## Overview

The Final Rule imposes a variety of new disclosure obligations on funds. The table below provides an overview of these new obligations and identifies some of the important aspects of the new disclosure requirements.

**Table I**

| <i>Form/disclosure requirement</i>                   | <i>Form N-PORT</i>  | <i>Form N-CEN</i>   | <i>Regulation S-X amendments</i>                                       | <i>Registration statement/Form N-CSR amendments</i>                         |
|--|---|---|--|---|
| Entities required to file or disclose, as applicable | All registered management investment companies (including ETFs organized as unit investment trusts) except money market funds and small business investment companies; each series must file separately   | All registered investment companies except face-amount certificate companies                  | All registered investment companies and business development companies | All registered management investment companies                              |
| Frequency of reporting/disclosure updates            | Monthly   | Annually  | Semi-annually in connection with shareholder reports                   | Annually for registration statements and semi-annually for closed-end funds |
| Filing deadline/timeline for disclosure updates      | No later than 30 days after month-end   | No later than 75 days after fiscal year-end (or calendar year-end for unit investment trusts) | Semi-annually in connection with issuance of shareholder report        | Annually for registration statements and semi-annually for closed-end funds |
| Time period covered by filing                        | Last business day, or last calendar day, of month. Must disclose information as calculated by fund for the reporting period's ending NAV (commonly, and as permitted by rule 2a-4, the first business day following the trade date, or "T + 1")                                 | Fiscal year   | Fiscal year or fiscal half-year covered by shareholder report          | Fiscal year   |
| Time when information becomes publicly available     | Form N-PORT filed for third month of a fund's fiscal quarter will be publicly available 60 days after filing (other than information that the form provides is not public). <sup>[4]</sup> Form N-PORT filed for first and second months of fund's fiscal quarter is not public | Immediately upon filing   | Immediately upon filing  | Immediately upon filing   |
| Filing format  | Structured data (XML) format  | Structured data (XML) format  | No changes   | No changes  |
| Compliance date                                      | June 1, 2018 for funds that are part of a complex with \$1 billion or more in assets; June 1, 2019 for all other funds  | June 1, 2018  | August 1, 2017   | August 1, 2017  |

## New Form N-PORT and the rescission of Form N-Q

### *Overview*

Form N-PORT will require registered management investment companies (mutual funds, closed-end funds and exchange-traded funds (ETFs)) as well as ETFs organized as unit investment trusts (UITs) (collectively referred to as “funds” for purposes of the discussion relating to Form N-PORT) to electronically file portfolio-wide and position-level information on a monthly basis with the SEC in a structured extensible markup language (XML) format<sup>[5]</sup>, no later than 30 days after each month’s end<sup>[6]</sup>. Money market funds operating in accordance with Rule 2a-7 under the Investment Company Act of 1940 (1940 Act) and small business investment companies (SBICs) are not required to file reports on Form N-PORT.

Information filed on Form N-PORT for the third month of each fiscal quarter of a fund will be publicly available 60 days after the end of the fund’s fiscal quarter. Information filed on Form N-PORT for the first and second month of each fiscal quarter will not be publicly available, although Form N-PORT explicitly provides that the SEC may make public information that is not identifiable to a specific fund or investment adviser. In response to comments received on the Proposed Rule, the SEC also has identified specific responses (and any related Explanatory Notes) that will remain non-public.

Form N-PORT requires reporting of information that will be helpful in understanding a fund’s investment strategies, including manner of implementation. Form N-PORT requires information on fund holdings, such as securities, commodities, currencies, derivatives and other investments. Further, Form N-PORT requires certain information about a fund’s use of securities lending, repurchase agreements and reverse repurchase agreements, as well as information regarding a fund’s over-the-counter derivatives transactions. In addition, Form N-PORT requires funds to calculate and report certain risk metrics that will reveal the fund’s sensitivity to changes in interest rates, credit spreads and asset prices, as a result of investments in derivatives or debt securities. Form N-PORT also requires funds to provide information regarding fund flows and the liquidity of fund positions. Instruction G to Form N-PORT provides that, in reporting information, a fund may respond using its own methodology and the conventions of its service providers, so long as the methodology and conventions are consistent with the way the fund reports internally and to current and prospective investors<sup>[7]</sup>. Each substantive part of the form is discussed in further detail below.

### *Form N-PORT, Part A: general information*

Form N-PORT requires certain identifying information about a fund. Funds offering multiple series will be required to file a separate report for each series, even if the information required to be provided for those series is identical and would be duplicative. Part A requires a fund to provide its name, 1940 Act file number, CIK number, Legal Entity Identifier (LEI)<sup>[8]</sup>, address and telephone number. If a fund has separate series, it will be required to report the name of the series, EDGAR series identifier and the LEI of the series completing the report. Funds also are required to disclose the date of fiscal year-end and the date as of which information is being reported.

### *Form N-PORT, Part B: information about the fund*

Form N-PORT requires information about a fund’s portfolio investments as of the close of the preceding month:

1. *Assets and liabilities:* A fund is required to report total assets, total liabilities and net assets. The fund also is required to separately report information about:

- Assets attributable to “miscellaneous securities”.
  - Assets invested in a Controlled Foreign Corporation (CFC) for the purpose of investing in certain types of instruments.
  - Borrowings attributable to amounts payable for notes payable, bonds and similar debt.
  - Payables for investments purchased either on a delayed delivery, when-issued or other firm commitment basis, or on a standby commitment basis.
  - The liquidation preference of any outstanding preferred stock issued by the fund.
2. *Portfolio-level risk metrics:* Form N-PORT requires certain funds to disclose various portfolio level risk metrics. If the average value of a fund’s debt securities positions for the previous three months, in the aggregate, exceeds 25 per cent or more of the fund’s net asset value (NAV), the fund is required to disclose the information regarding portfolio-level risk metrics in response to Item B.3. The notional value of various derivative instruments for which the underlying reference asset(s) are debt securities or interest rates is included when calculating the value of a fund’s debt securities positions. The SEC acknowledged in the Adopting Release that using a three-month average value (rather than value as percentage of NAV at month-end), and increasing the threshold from 20 to 25 per cent, would relieve more funds from having to monitor on a monthly basis whether the disclosure requirement is triggered, while still providing the Commission with useful measurements of duration and spread duration by funds that make investments in debt instruments.

The risk metrics include measurements of interest rate risk and credit spread risk. A fund is required to calculate the change in value of its portfolio resulting from both a one basis point change (DV01) and a one hundred basis point change (DV100) in interest rates (*e.g.*, 0.01 and 1.0 per cent, respectively) for specified maturities. These calculations are required to be made for each type of currency for which the fund had a value of 1 per cent or more of the fund’s NAV. Funds are required to calculate DV01 and DV100 for each of the following maturities: 3-month, 1-year, 5-year, 10-year, and 30-year. The Final Rule utilizes five key rates for purposes of calculating DV01 and DV100, while the Proposed Rule utilized 11 key rates<sup>[9]</sup>. The SEC noted that decreasing the number of key rates would reduce the reporting burden on funds and still provide the SEC staff with sufficient information regarding how debt portfolios would be impacted by changes to interest rates and credit spreads.

A fund also is required to calculate the change in the value of its portfolio resulting from a one basis point change in credit spreads (SDV01), where the shift is applied to the option-adjusted spread at the same maturities for calculating interest rate risk, aggregated by non-investment grade and investment grade exposures. Form N-PORT does not provide a definition for the terms “investment grade” and “non-investment grade”; however, as noted above, Instruction G provides funds with flexibility in determining what constitutes “investment grade”.

3. *Securities lending:* A fund is required to disclose the full name and LEI of each borrower in a securities lending arrangement, as well as the aggregate value of all securities on loan to that borrower. A fund also is required to disclose certain information regarding any non-cash collateral provided by a securities lending counterparty, including the aggregate principal amount and aggregate value of each type of non-cash collateral received for loaned securities, which is not treated as a fund asset for purposes of the Schedule of Portfolio Investments in Part C of Form N-PORT. Funds also must identify the type of investment that most closely represents the non-cash collateral.

4. *Return information:* A fund is required to report monthly total returns for each of the preceding three months, using the same calculation method currently used to report return information in the performance table of the risk-return summary of the fund's prospectus and sales materials. Multi-class funds are required to report return information for each class of shares.

Form N-PORT also requires funds to disclose for each of the preceding three months the monthly net realized gain (or loss) and net change in unrealized appreciation (or depreciation) arising from certain derivative contracts<sup>[10]</sup> and, separately, from investments other than derivatives<sup>[11]</sup>.

5. *Flow information:* Similar to information currently reported on Form N-SAR, Form N-PORT requires a fund to separately report the aggregate dollar amounts for sales and redemptions/repurchases of fund shares during each of the preceding three months. Specifically, a fund is required to report the total NAV of: (i) shares sold (including exchanges but excluding reinvestment of dividends and distributions); (ii) shares sold in connection with reinvestments of dividends and distributions; and (iii) shares redeemed or repurchased, including exchanges. If shareholders of a fund hold shares through an omnibus account, the fund can use net sales, or redemptions/repurchases from such omnibus accounts.

#### ***Form N-PORT, Part C: schedule of portfolio investments***

Form N-PORT requires a fund to disclose certain information about each of its portfolio investments and the portfolio investments of any consolidated subsidiaries (e.g., CFCs), as of the close of the preceding month.

- *Identification of investment:* With respect to each investment, a fund is required to report the name of issuer, the LEI (if available) of the issuer<sup>[12]</sup>, title of the issue or description of the investment, CUSIP (if any), and at least one other identifier and the type of identifier used<sup>[13]</sup>.
- *Amount of each investment:* With respect to each investment, a fund is required to report the balance (e.g., number of shares held, principal amount, units, number of contracts), value in US Dollars, and percentage value compared to the net assets of the fund. Funds will also report the currency in which an investment is denominated and, if not denominated in US Dollars, the exchange rate used to calculate value.
- *Payoff profile:* A fund is required to indicate whether it is holding an investment long, short, or not applicable (N/A)<sup>[14]</sup>.
- *Asset and issuer type:* A fund is required to report the asset and issuer type for each investment selected from categories set forth in Form N-PORT, which are based on categories required to be reported by private funds on Form PF.
- *Country of investment or issuer:* A fund is required to disclose the country in which the issuer of each investment is organized, using the ISO country code, and, if different, the ISO country code that corresponds to the country of investment or issuer based on the concentrations of the investment's risk and economic exposure. The country of risk and economic exposure will be non-public information.
- *Restricted security:* A fund is required to indicate whether each investment is a restricted security.
- *Fair value hierarchy:* A fund is required to report, for each investment, the level within the fair value hierarchy in which the fair value measurements fall pursuant to

US Generally Accepted Accounting Principles (GAAP) (*i.e.*, Level 1, Level 2 or Level 3)[15].

- *Securities lending*: With respect to each investment, a fund is required to report whether: (i) any amount of the investment represents reinvestment of cash collateral received for loaned securities and, if so, the value of the investment representing cash collateral; (ii) any portion of the investment represents non-cash collateral that is treated as a fund asset and is received for loaned securities and, if so, the value of the securities representing the non-cash collateral; and (iii) any portion of the investment is on loan by the fund and, if so, the value of the security on loan.

Form N-PORT also requires funds to report additional detailed information regarding: (i) debt and convertible securities; (ii) repurchase agreements and reverse repurchase agreements; and (iii) derivatives.

- *Debt securities*: With respect to each debt security held, a fund is required to report: (i) the maturity date; (ii) the coupon (identifying the coupon type as either fixed, floating, variable or none); (iii) the annualized rate; (iv) whether the security is currently in default; (v) whether the interest payments are currently in arrears; (vi) whether any coupon payments have been legally deferred; and (vii) whether any portion of the interest is paid in kind.
- *Convertible securities*: With respect to each convertible security held, a fund is required to report: (i) whether the conversion is mandatory or contingent; (ii) information about the asset into which the debt is convertible; (iii) conversion ratio; and (iv) delta (if applicable)[16].
- *Repurchase and reverse repurchase agreements*: A fund is required to report for each repurchase or reverse repurchase agreement: (i) whether the instrument is a repurchase agreement (*i.e.*, fund is the cash lender and recipient of collateral) or a reverse repurchase agreement (*i.e.*, fund is the cash borrower and poster of collateral); (ii) whether the transaction is cleared by a central counterparty[17]; (iii) whether the agreement is tri-party; (iv) the maturity date; (v) the principal amount; (vi) the value of collateral; and (vii) the category of investment that closely represents the collateral[18].
- *Derivative contracts*: With respect to derivative contracts, a fund is required to identify and report: (i) the type of derivative instrument (forward, future, option, swaption, swap (including but not limited to total return swaps, credit default swaps and interest rate swaps), warrant, and other[19]); (ii) the name and LEI of the counterparty (including central counterparty, if any); (iii) a description of the reference instrument, if applicable (including the name of the issuer, title of issue and relevant securities identifier)[20]; and (iv) any unrealized appreciation or depreciation[21].

In addition to the information required for all derivative contracts discussed above, a fund is required to report information with respect to: (i) options, warrants, and options on a derivative; (ii) futures and forwards (other than forward foreign currency contracts); (iii) forward foreign currency contracts and foreign currency swaps; (iv) swaps (other than foreign exchange swaps); and (v) all other derivatives that do not fall into the enumerated categories.

- *Options, warrants, and options on a derivative*: A fund is required to report: (i) type (*e.g.*, put or call); (ii) payoff profile (*e.g.*, written or purchased); (iii) number of shares or principal amount of underlying reference instrument per contract; (iv) exercise price or rate; (v) expiration date; and (vi) delta.
- *Futures and forwards (other than forward foreign currency contracts)*: A fund is required to report the payoff profile (*e.g.*, long or short), expiration date, and aggregate notional amount or contract value on the trade date.



- *Forward currency contracts and foreign currency swaps*: A fund is required to report the amount, a description of any currency sold or purchased, and the settlement date.
- *Swaps (other than foreign exchange swaps)*: A fund is required to report: (i) the description and terms of payments, necessary for a user of financial information to understand the terms of payments to be made and received; (ii) financing rate; (iii) floating coupon rate; (iv) fixed coupon rate; (v) payment frequency; (vi) termination or maturity date; (vii) upfront payments or receipts; and (viii) notional amount.
- *All other derivatives*: A fund is required to report: (i) the description of the terms and nature of the investment, sufficient for a user of financial information to understand the nature and terms; (ii) currency; (iii) payment terms; (iv) payment rates; (v) call or put feature; (vi) exercise price; (vii) termination or maturity (if any); (viii) notional amount(s); and (ix) delta.

#### ***Form N-PORT, Part D: miscellaneous securities***

As noted above, a fund may report certain investments as “miscellaneous securities”, subject to certain conditions<sup>[22]</sup>. Unless otherwise indicated, funds will not report information related to these investments in Part C, but will instead report such information in Part D. Form N-PORT requires funds to provide, on an investment-by-investment basis, the same information about each security as required in Part C, as discussed above. Funds need only identify miscellaneous securities in reports filed for the last month of each fiscal quarter. Information reported in Part D will not be made public.

#### ***Form N-PORT, Part E: explanatory notes (if any)***

Form N-PORT permits, but does not require, a fund to provide explanatory notes relating to the filing. Any notes provided in the public filings of the form (*i.e.*, those filings made during the third month of a fund’s fiscal quarter) will be publicly available, whereas notes provided in other filings will be non-public. Explanatory notes related to items that the SEC does not intend to make public, as identified in Instruction F of Form N-PORT (*e.g.*, delta), will not be made public. A fund may use Part E to provide any information it believes will be helpful in understanding information reported in response to any other item of Form N-PORT. For example, a fund may use Part E to explain any of the assumptions that were made in responding to any other item of Form N-PORT.

#### ***Form N-PORT, Part F: exhibits***

With respect to Form N-PORT filings for the end of the first and third quarters of a fund’s fiscal year, the fund is required to include, no later than 60 days after the end of the reporting period, an exhibit disclosing the fund’s complete portfolio holdings as of the close of the period covered by the report. The information in this exhibit will not be audited or certified and will be presented in accordance with Regulation S-X, as amended. In other words, the schedule will be in a format similar to that currently used in Form N-Q.

#### ***Rescission of Form N-Q and amendments to certification requirements for Form N-CSR***

Given that the information to be reported on Form N-PORT will be duplicative of Form N-Q, the SEC rescinded Form N-Q. This rescission eliminates certifications as to the accuracy of the portfolio schedules reported for the first and third fiscal quarters. However, because Form N-CSR currently requires the certifications for portfolio schedules to be reported for only the second and fourth fiscal quarters, the SEC adopted amendments to Form N-CSR to require that the certifications cover the full semi-annual period.



## New Form N-CEN and the rescission of Form N-SAR

### *Overview*

The SEC adopted new Form N-CEN, which replaces Form N-SAR for census-type information. The SEC also rescinded Form N-SAR. The Final Rule requires, as proposed, all registered investment companies other than face-amount certificate companies (collectively referred to as “funds” for purposes of the discussion related to Form N-CEN) to file reports on Form N-CEN in XML format. Series companies will be required to file a single report on Form N-CEN covering all series, similar to the manner in which funds file reports on Form N-SAR. As discussed below, different types of funds will be required to complete different sections of Form N-CEN.

The SEC adopted, as proposed, the requirement that all funds file reports on new Form N-CEN annually, as opposed to semi-annually (as was required for reports on Form N-SAR). Persuaded by comments received in response to the Proposed Rule’s 60-day filing deadline, the SEC extended the filing deadline to 75 days after the end of a fund’s fiscal year-end for management companies and calendar year-end for UITs[23]. As stated in the instructions to Form N-CEN, funds that offer multiple series with different fiscal year-ends must file a report on Form N-CEN for each fiscal year-end responding to (i) Parts A, B, and G, and (ii) Part C and Part E (if Part E is applicable) as to only those series with the fiscal year-end covered by the report. UITs that offer multiple series will be required to file a single report on Form N-CEN covering each series as of the end of the calendar year.

### *Form N-CEN, Part A: general information and Part B: information about the fund*

All funds will be required to complete Part A and Part B of Form N-CEN. Part A requires general information about the covered reporting period. Part B requires certain background information and identifying information about the fund, to allow the SEC staff to efficiently categorize filers by fund type. Part B also requires other kinds of information that may be useful to the SEC staff in monitoring the fund industry. Specifically, Part B requires a fund to disclose, among other information:

- CIK file number and LEI.
- Location of its books and records[24].
- Whether it issues a class of securities registered under the Securities Act of 1933.
- Information about each director/trustee, including his or her name, CRD number (if any), whether he or she is an “interested person” (as defined in section 2(a)(19) of the 1940 Act), and the 1940 Act file number of any other fund for which he or she serves as director.
- Information about its chief compliance officer (CCO), including information as to whether the CCO is employed or compensated by a third-party[25].
- Whether there were any material legal proceedings to which the fund was a party, or any of the fund’s property was subject, during the reporting period.
- Whether there were any claims with respect to the fund filed under a fidelity bond during the reporting period.
- Information regarding the fund’s receipt of “financial support” from an affiliated entity[26].
- Whether the fund relied on exemptive orders granted to the fund by the Commission during the reporting period.
- Identifying information for the fund’s principal underwriter and independent public accountant, and whether there have been any changes to the fund’s principal underwriter or independent public accountant since the last filing[27].

- Whether there were any material changes in the method of valuation of the fund's assets, changes in accounting principles or practices, or any NAV error corrections during the reporting period.

***Form N-CEN, Part C: additional questions for management investment companies***

Part C of Form N-CEN will be completed by funds other than SBICs. Like Form N-SAR, Form N-CEN requires general identifying information about the fund and any of its series; however, unlike Form N-SAR, Form N-CEN requires disclosure of specific information about the classes of open-end management companies. Among other requirements, Part C requires a fund to disclose:

- What type of fund it is.
- Whether it seeks to operate as a non-diversified company as defined in Section 5(b)(2) of the 1940 Act.
- In the case of an index fund (*i.e.*, a fund, including an ETF, that seeks to track the performance of a specified index), the fund's "tracking difference"[28], "tracking error"[29], and whether the index was constructed exclusively for the fund or constructed by affiliated service providers of the fund.
- Whether it invests in a CFC for the purpose of investing in certain types of instruments, such as commodities.
- Certain information about its securities lending activities, including: whether any borrower has defaulted[30]; the identify of each securities lending agent and whether the securities lending agent is a first- or second-tier affiliate of the fund; the identify of each cash collateral manager and whether the cash collateral manager is a first- or second-tier affiliate of the fund; and any revenue sharing splits or other fees of the fund's securities lending arrangements.
- Information relating to fund expense limitation arrangements, with greater specificity than is currently required on Form N-SAR. A fund is required to disclose: any expense limitation arrangements in place for the fund during the reporting period; whether any amounts had been waived or reduced pursuant to an arrangement during the reporting period; whether the fees waived are subject to recoupment; and whether any expenses previously waived were recouped during the reporting period.

***Form N-CEN, Part D: additional questions for closed-end management investment companies and small business investment companies***

Similar to Form N-SAR, and as proposed, Form N-CEN requires closed-end funds and SBICs to report additional information in Part D. SBICs are required to complete Part D in lieu of Part C, while closed-end funds will complete Part C and Part D. There are few differences between the disclosures required by Part D of Form N-CEN and those currently required by Form N-SAR, which requires disclosure of, among other things: the types of securities issued; repurchases of securities; defaults on long-term debt; and dividends in arrears. However, one difference is that Form N-CEN (unlike Form N-SAR) requires closed-end funds and SBICs to disclose information relating to rights offerings and secondary offerings, including whether there was such an offering during the reporting period and the type of security involved.

***Form N-CEN, Part E: additional questions for exchange-traded funds and exchange-traded managed funds***

Part E relates specifically to ETFs. Part E requires information identifying the exchange on which the ETF is listed and its ticker symbol. In addition, Part E requires certain identifying information for each authorized participant of the ETF, including the

authorized participant's name, SEC file number, CRD number, and LEI (if any). Part E also requires disclosure regarding the dollar value of ETF shares purchased during the reporting period, as well as the dollar value of shares redeemed from the ETF during the reporting period[31].

Part E of Form N-CEN requires that ETFs disclose specific information about creation units and primary market transactions. ETFs are required to report, as to creation units purchased by authorized participants during the reporting period, and as to creation units purchased by authorized participants that were fully or partially composed of cash, the average transaction fee: (i) charged in dollars per creation unit; (ii) charged for one or more creation units on the same business day; and (iii) charged as a percentage of the value of the creation unit. ETFs are required to report parallel information for the redemption of creation units by authorized participants. Part E also requires that a UIT operating as an index fund (*i.e.*, as a fund that seeks to track the performance of a specified index) must disclose certain information regarding performance differences between the UIT and the performance of its benchmark index.

#### ***Form N-CEN, Part F: additional questions for unit investment trusts***

Part F, adopted as proposed, requires information specific to UITs. Part F of Form N-CEN requires certain identifying information, including identifying information about the UIT's depositors and administrators. Form N-CEN differentiates between whether or not a UIT is a separate account of an insurance company, and requires responses to different sets of questions depending on whether it is a separate account of an insurance company. Form N-CEN also requires certain new information be reported by separate accounts offering variable annuity and variable life insurance contracts.

#### ***Form N-CEN, Part G: attachments***

The SEC adopted Part G substantially as proposed. Like Form N-SAR, Part G of Form N-CEN requires descriptive attachments to the filing; however, the SEC sought to limit the number of attachments to the form in order to simplify the filing process while simultaneously maximizing the amount of information received in XML format. All of the attachments that will be required under Form N-CEN are currently required by Form N-SAR, except for the attachment related to the provision of financial support. If a fund has received financial support, it will be required to provide detailed information about the financial support arrangement.

## **Amendments to regulation S-X**

### ***Overview***

Regulation S-X prescribes the content and form of financial statements to be included in registration statements and shareholder reports for registered investment companies and business development companies (referred to as "funds" for purposes of the discussion in this section)[32]. The SEC adopted amendments to Regulation S-X, many of which are consistent with the enhanced reporting regime outlined in Form N-PORT and Form N-CEN, particularly with respect to disclosure pertaining to a fund's derivative contracts. Specifically, the amendments require additional disclosures regarding a fund's derivative investments, which must be prominently placed in a schedule in the fund's financial statements (rather than as a schedule in the notes to the financial statements).

### ***Enhanced derivatives disclosure***

The SEC adopted amendments to Article 12 of Regulation S-X, which set forth new, standardized schedules for reporting position-level information as to open futures contracts, open forward foreign currency contracts, and open swap contracts. The

amendments also modify the current disclosure requirements applicable to the schedule of purchased and written options contracts. Further, the amendments implement new instructions regarding the format and display of disclosures regarding derivative contracts; these instructions are consistent with the instructions for Rule 12-12 and current Rule 12-13. Please refer to the [Appendix](#) for details regarding the derivatives disclosure.

#### ***Additional regulation S-X Amendments***

The Final Rule implements several other amendments to Regulation S-X, including:

- Adding an instruction to Rule 12-12 that will require a fund to indicate the interest rate or preferential dividend rate and maturity rate, as applicable, for certain enumerated debt instruments<sup>[33]</sup>.
- Revising instruction 4 to Rule 12-13 and Rule 12-13C to no longer require disclosure of the counterparty for both exchange-traded options and swaps and centrally cleared options and swaps.
- Amending the instructions to Rule 12-12 to require funds to indicate whether any portion of a security held in connection with open put or call option contracts, or loans for short sales, is on loan.
- Amending Rule 12-14 to require funds to disclose additional information regarding their investments in, and advances to, affiliates.

#### **Amendments to forms regarding securities lending activities**

In the Final Rule, the SEC adopted amendments to Forms N-1A, N-3, and N-CSR that require registered management investment companies (referred to as “funds” for purposes of the discussion in this section) to disclose certain information regarding their securities lending activities in their registration statements (or their Form N-CSR filings, in the case of closed-end funds). The Proposed Rule would have required the disclosure of information relating to securities lending activities in a fund’s financial statements; however, the SEC was persuaded by commenters’ views that including such disclosure in a fund’s financial statements could dilute the significance of other financial statement disclosures. As such, the Final Rule requires funds to include these disclosures in their Statement of Additional Information (SAI) and closed-end funds to include these disclosures in response to new Item 12 of Form N-CSR. The Final Rule amends Forms N-1A and N-3, as well as Form N-CSR (for closed-end funds only), rather than Regulation S-X, as proposed. In response to concerns expressed by some commenters as to the Proposed Rule’s requirement that terms governing compensation of the securities lending agent be made publicly available, the SEC modified the Proposed Rule to require disclosure of backward-looking actual compensation levels (rather than potentially sensitive, negotiated contractual terms).

#### ***Requirement to disclose securities lending income, expenses and services***

The Final Rule requires disclosure of the following information regarding a fund’s securities lending activities:

1. Gross income from securities lending activities, including income from cash collateral reinvestment<sup>[34]</sup>.
2. The dollar amount of all fees and/or compensation paid by the fund for securities lending activities and related services, including:

- Fees paid to a securities lending agent from a revenue split.
  - Fees paid for any cash collateral management service (including fees deducted from a pooled cash collateral reinvestment vehicle) that are not included in a revenue split.
  - Administrative fees not included in a revenue split.
  - Indemnification fees not included in a revenue split.
  - Rebate (paid to borrower).
  - Other fees not included in a revenue split.
3. The aggregate fees/compensation for securities lending activities.
  4. Net income from securities lending activities.

A fund also is required to provide a description of the services included in the fund's arrangement with its securities lending agent, which the SEC specified should be based on the services actually furnished to the fund in its most recent fiscal year<sup>[35]</sup>.

### Option for website transmission of shareholder reports – not adopted by the SEC

The Proposed Rule included a proposal to adopt new Rule 30e-3 under the 1940 Act, which would have permitted, but not required, a fund to satisfy current shareholder report delivery obligations by making the reports and certain other materials accessible on the fund's website. In proposing new Rule 30e-3, the SEC noted that funds and their shareholders would "benefit from the reductions in related printing and mailing costs". The SEC acknowledged that there likely would be a significant minority of investors who would prefer to continue receiving shareholder reports in paper and, accordingly, the SEC drafted proposed Rule 30e-3 in a manner to protect an investor's choice to continue to receive printed reports. Reliance on proposed Rule 30e-3 would have been subject to certain conditions, including those regarding: (i) the availability of the report and other related materials; (ii) shareholder consent; (iii) notice to shareholders of availability; (iv) delivery upon request; and (v) restrictions on use of a summary schedule of investments.

After receiving comments from over 900 commenters on proposed Rule 30e-3, the SEC decided not to take action to adopt the proposal at this time. The SEC stated that a number of comments received on the proposal raised issues regarding the expected costs and benefits associated with encouraging internet delivery of shareholder reports, and the SEC acknowledged that these issues deserve further consideration before any final action is taken with respect to proposed Rule 30e-3.

### Conclusion

The Final Rule will have a significant effect on many funds. Funds will experience a substantially increased reporting burden, both with respect to the frequency of reporting and the granularity of information required. Fund managers and fund service providers should begin evaluating the impact of the Final Rule and the processes that will need to be implemented to prepare filings on new Forms N-PORT and N-CEN, as well as assessing the changes that will need to be made to existing fund disclosure practices in response to the amendments to Regulation S-X and certain forms.

### Notes

1. Investment Company Reporting Modernization, Release No. IC-32314 (Oct. 13, 2016) (Adopting Release). SEC Chair Mary Jo White and Commissioner Kara Stein voted in favor of the Final Rule, and Commissioner Michael Piwowar voted against the Final Rule.

2. See, e.g., Interactive Data for Mutual Fund Risk/Return Summary, Release No. IC-28617 (Feb. 11, 2009).
3. Investment Company Reporting Modernization, Release No. IC-31610 (May 20, 2015).
4. The SEC does not intend to make public any information reported on Form N-PORT with respect to country of risk and economic exposure (Item C.5.b), delta (Items C.9.f.5, C.11.c.vii, or C.11.g.iv), miscellaneous securities (Part D), or explanatory notes related to any of those topics (Part E) that are identifiable to any particular fund or investment adviser.
5. The SEC is requiring that XML format be used for Form N-PORT filings, as is currently required for filings made on Form N-MFP and Form PF.
6. In response to comments on the Proposed Rule that expressed concern as to the reporting of information on a "trade date plus zero" basis, the SEC adopted a "trade date plus one" requirement for holdings reported on Form N-PORT.
7. Instruction G is similar to Instruction 15 of Form PF, which allows a reporting entity to use its own methodologies and conventions in reporting information.
8. The LEI is a unique identifier associated with a single corporate entity by a utility endorsed by the Global LEI Regulatory Oversight Committee or accredited by the Global LEI Foundation. Funds that have not yet obtained an LEI will need to obtain one from a Global Markets Entity Identifier Utility for a fee. Funds must pay an annual fee to maintain the LEI.
9. Under the Proposed Rule, funds would have been required to make calculations for each of the following maturities: 1-month, 3-month, 6-month, 1-year, 2-year, 3-year, 5-year, 7-year, 10-year, 20-year and 30-year.
10. Funds are required to report this information both by asset category (e.g., commodity contracts, credit contracts, equity contracts) and type of derivative instrument (e.g., forward, future, option, swap).
11. The Adopting Release indicates that this disclosure is modeled after Financial Accounting Standards Board Accounting Series Codification 815.
12. For a fund's holding of a particular portfolio investment that is a series of another fund, the reporting fund must disclose the LEI of the specific series held.
13. The identifiers include ISIN, ticker symbol (if ISIN is not available) or another unique identifier.
14. Form N-PORT provides that, for derivatives, a fund should respond "N/A" because payoff profile is included in Item B.10.
15. As adopted, Form N-PORT allows funds to report "N/A" in response to this item if an investment does not have a fair value level hierarchy assigned to it pursuant to FASB Accounting Standards Update 2015-07.
16. Delta is the ratio of: (i) the change in value of the option, to (ii) the change in value of the asset into which the debt is convertible. In response to comments, the SEC decided it will not publicly disclose data on delta.
17. If the transaction is cleared by a central counterparty, a fund will provide only the name of the counterparty; however, if the agreement is not cleared by a central counterparty, a fund also will provide the name and LEI of the over-the-counter counterparty.
18. The categories include: asset-backed securities; agency collateralized mortgage obligations; agency debentures and agency strips; agency mortgage-backed securities; private label collateralized mortgage obligations; corporate debt securities; equities; money market funds; US Treasuries (including strips); and other instruments. In the case of an "other instrument", a fund will need to provide a brief description, including whether it is a collateralized debt obligation, municipal debt, whole loan, or international debt.
19. If a fund responds "other", it must provide a brief description of the instrument.

20. If the reference instrument is a derivative, a fund will report the type of derivative and provide all information required to be reported on Form N-PORT for that type. If the reference instrument is an index or custom basket for which the index's or custom basket's components are publicly available on a website and updated no less than quarterly, a fund will be required to identify the index and provide the index identifier, if any. If the index's or custom basket's components are not publicly available, and the notional amount of the derivative represents 1 per cent or less of a fund's NAV, the fund will be required to provide only a narrative description of the index. If the index's or custom basket's components are not publicly available, and the notional amount of the derivative represents more than 1 per cent and up to 5 per cent of a fund's NAV, the fund must report the top 50 components of the index or basket as well as those components that exceed 1 per cent of the notional value of the index or basket. If the index's or custom basket's components are not publicly available, and the notional amount of the derivative represents more than 5 per cent of a fund's NAV, the fund will be required to provide: (i) name of the component; (ii) identifier of the component; (iii) number of shares or notional amount or contract value as of the trade date; and (iv) value of every component in the index or custom basket. As a result of these disclosure requirements, a fund may need to modify its derivative contract to allow for the disclosure of certain information.
21. A fund should report depreciation as a negative number.
22. A fund may report information for securities in an aggregate amount not exceeding 5 per cent of its total assets as "miscellaneous securities" in one amount in Part D in lieu of reporting those securities in Part C, provided that the securities so listed: are not restricted; have been held for not more than one year prior to the date of the related balance sheet; and have not previously been reported by name to shareholders or set forth in any registration statement, application or report to shareholders or otherwise made available to the public.
23. If a fund changes its fiscal year, a report filed on Form N-CEN may cover a period shorter than 12 months, but it may not cover a period longer than 12 months or a period that overlaps with a period covered by a previously filed report.
24. Books and records information is currently required to be reported on fund registration forms in a non-structured format. The SEC believes that having the location of a fund's books and records filed on Form N-CEN will increase the Commission's efficiency in preparing for exams. The SEC adopted amendments to Forms N-1A, N-2, N-3, N-4, and N-6 to eliminate the requirement that a fund disclose the location of its books and records on those forms, provided such information is disclosed in the fund's most recent Form N-CEN filing.
25. Specifically, if the CCO is compensated or employed by any person other than the fund, or an affiliated person of the fund, for providing CCO services, the fund must provide the name of the person and his or her IRS Employer Identification Number.
26. The Final Rule modifies the instruction to reflect that a purchase of a defaulted or devalued security at fair value need only be characterized as "financial support" for purposes of Form N-CEN if it is intended to increase or stabilize the value or liquidity of the fund's portfolio.
27. Under the Proposed Rule, if the independent public accountant changed since the last filing, the fund would have been required to provide a detailed narrative attachment to Form N-CEN reporting this change, along with the predecessor accountant's letter reporting the change. In response to commenters' concerns about the potentially significant time lapse between a change in accountant and the filing of Form N-CEN, the SEC adopted an amendment to Form N-CSR that requires this attachment to be included on Form N-CSR.
28. "Tracking difference" refers to the difference between an index fund's total return during the reporting period and the index's return during the reporting period.
29. "Tracking error" refers to a measurement of the volatility of the tracking difference from day-to-day over the course of the reporting period.
30. The Final Rule modifies the Proposed Rule by requiring disclosure of failures to return loaned securities that result in the fund or its securities lending agent having to liquidate collateral pledged to secure the loaned securities or the fund otherwise being adversely impacted. Other



adverse impacts to a fund include: a loss to the fund if collateral and indemnification were not sufficient to replace the loaned securities or their value; the fund's ineligibility to vote shares in a proxy; or the fund's ineligibility to receive a direct distribution from the issuer. The SEC believes that this modification will allow it to differentiate between defaults that have the potential to expose the fund and its shareholders to harm and technical defaults.

31. Part E also requires an ETF to disclose whether it required an authorized participant to post collateral to the ETF or any of its designated services providers in connection with any purchase or redemption transactions of ETF shares during the reporting period.
32. There were only certain limited amendments that apply to UITs and face-amount certificate companies.
33. When disclosing the interest rate for variable rate securities, a fund must describe the reference rate and spread as well as provide the end of period interest rate for each investment, or include disclosure of each reference rate at the end of the period.
34. The SEC clarified that gross income may also include: negative rebates; loan fees paid by borrowers when collateral is non-cash; management fees from a pooled cash collateral reinvestment vehicle that are deducted from the vehicle's assets before income is distributed; and any other income.
35. Examples of the types of securities lending services funds may wish to disclose include, among others: locating borrowers; monitoring daily the value of the loaned securities and collateral; requiring additional collateral as necessary; cash collateral management; qualified dividend management; negotiation of loan terms; selection of securities to be loaned; recordkeeping and account servicing; monitoring dividend activity and material proxy votes relating to loaned securities; and arranging for return of loaned securities to the fund at loan termination.
36. If the index's or custom basket's components are not publicly available, and the notional amount of the option contract does not exceed 1 per cent of a fund's NAV, the fund will be required to identify the index or basket. If the index's or custom basket's components are not publicly available, and the notional amount of the derivative exceeds 1 per cent of a fund's NAV, the fund must report the top 50 components of the index or basket as well as those components that exceed 1 per cent of the notional value of the index or basket.
37. This is consistent with investments categorized as Level 3 in the fair value hierarchy pursuant to US GAAP.
38. *See supra* n.36 (discussing the *de minimus* threshold for reporting index components that are not publicly available).

## Appendix. Regulation S-X derivatives disclosures

### *Open option contracts written – new Rule 12-13*

New Rule 12-13 requires funds to disclose additional information regarding their open written option contracts. The same disclosures will apply to purchased options. The table below summarizes the changes applicable to open option contracts reported under current Rule 12-12B and new Rule 12-13 (**Bold** indicates a change or new item; ~~strikethrough~~ indicates that the item is no longer reported).

| <i>Current Rule 12-12B</i> | <i>New Rule 12-13</i>              |
|----------------------------|------------------------------------|
| Name of issuer             | <b>Description of the contract</b> |
|                            | <b>Counterparty</b>                |
| Number of contracts        | Number of contracts                |
|                            | <b>Notional amount</b>             |
| Exercise price             | Exercise price                     |
| Expiration date            | Expiration date                    |
| Value                      | <b>Value</b>                       |

The Final Rule notes that if an investment contains any sort of optionality (e.g., a swaption), funds will be required to disclose the investment under both the swaps rule (new Rule 12-13C) and the options rule (new Rule 12-13). If the description of the contract includes an underlying investment tied to an index, funds will follow disclosure requirements that differ from those of Form N-PORT[36].

Additional instructions and amendments to the instructions to Rule 12-13 are applicable across all derivatives reporting schedules, in order to maintain consistency in reporting. The instructions require funds to indicate if an investment cannot be sold because of restrictions or conditions imposed on the investment or if an investment's value was determined using "significant unobservable inputs"[37].

### *Open futures contracts – new Rule 12-13A*

New Rule 12-13A requires funds to disclose additional information regarding open futures contracts. The SEC proposed, but decided not to adopt, a new instruction which would have required funds to reconcile the total of the unrealized appreciation/depreciation column to the total variation margin receivable or payable on the related balance sheet. The table below summarizes the changes applicable to open futures contracts reported under current Rule 12-13 and new Rule 12-13A (Italic indicates a change or new item).

| <i>Current Rule 12-13</i>            | <i>New Rule 12-13A</i>               |
|--------------------------------------|--------------------------------------|
| Description of the contract          | Description of the contract          |
| Number of contracts                  | Number of contracts                  |
| Expiration date                      | Expiration date                      |
|                                      | <b>Notional amount</b>               |
|                                      | <b>Value</b>                         |
| Unrealized appreciation/depreciation | Unrealized appreciation/depreciation |

### *Open forward foreign currency contracts – new Rule 12-13B*

The SEC adopted as proposed new Rule 12-13B, which requires funds to disclose additional information regarding their open forward foreign currency contracts, including whether a foreign currency contract cannot be sold due to restrictions or if the foreign currency contract is an illiquid investment. The table below summarizes the changes applicable to open forward foreign currency contracts reported under current Rule 12-13 and new Rule 12-13B (Italic indicates a change or new item).

| <i>Current Rule 12-13</i>                          | <i>New Rule 12-13B</i>                             |
|--|--|
| Amount and description of currency to be purchased | Amount and description of currency to be purchased |
| Amount and description of currency to be sold      | Amount and description of currency to be sold      |
|  | <b>Counterparty</b>                                |
| Settlement date                                    | Settlement date                                    |
| Unrealized appreciation/depreciation               | Unrealized appreciation/depreciation               |

### *Open swap contracts – new Rule 12-13C*

New Rule 12-13C requires funds to disclose additional information regarding their open swap contracts, including whether a swap contract cannot be sold due to restrictions or if the swap contract is an illiquid investment. Additionally, for swap contracts with an underlying investment tied to an index, funds will follow the disclosure requirements as provided by new Rule 12-13[38]. The table below summarizes the changes applicable to open swap contracts reported under current Rule 12-13 and new Rule 12-13C (Italic indicates a change or new item).

| <i>Current Rule 12-13</i>   | <i>New Rule 12-13C</i>  |
|---|---|
| Description and terms of payments to be received from another party | Description and terms of payments to be received from another party |
| Description and terms of payments to be made to another party       | Description and terms of payments to be made to another party       |
|   | <b>Counterparty</b>   |
| Maturity date   | Maturity date   |
| Notional amount   | Notional amount   |
|   | <b>Value</b>  |
|   | <b>Upfront payments/receipts</b>                                    |
| Unrealized appreciation/depreciation                                | Unrealized appreciation/depreciation                                |

### Corresponding author

Stephen Cohen can be contacted at: [stephen.cohen@dechert.com](mailto:stephen.cohen@dechert.com)

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