

May 5, 2020

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

Re: *Request for Comments on Fund Names (File No. S7-04-20)*

Dear Ms. Countryman:

The Investment Company Institute<sup>1</sup> commends the Commission for its recent request for comment on the framework for addressing names of registered investment companies and business development companies under Rule 35d-1 under the Investment Company Act of 1940 (“Names Rule”) and the antifraud provisions of the Federal securities laws.<sup>2</sup> We appreciate the Commission’s ongoing efforts to improve the investor experience and modernize regulatory approaches.

Registered investment companies (generally, “funds”) managed \$22.8 trillion in total net assets as of March 2020, largely on behalf of more than 100 million retail investors.<sup>3</sup> In 2001, when the Names Rule was adopted, funds managed \$7.2 trillion in total net assets.<sup>4</sup> The share of household assets in funds stands at 23% today, growing from 18% in 2001.<sup>5</sup> Today, the majority of fund net assets are in equity funds. Index-based funds have grown to 39% of industry assets in long-term mutual funds and

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<sup>1</sup> The Investment Company Institute (“ICI”) is the leading association representing regulated funds globally, including mutual funds, exchange-traded funds (“ETFs”), closed-end funds, and unit investment trusts in the United States, and similar funds offered to investors in jurisdictions worldwide. ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. ICI’s members manage total assets of US\$22.1 trillion in the United States, serving more than 100 million US shareholders, and US\$6.5 trillion in assets in other jurisdictions. ICI carries out its international work through ICI Global, with offices in London, Hong Kong, and Washington, DC.

<sup>2</sup> See Request for Comments on Fund Names, SEC Release No. IC-33809 (Mar. 2, 2020), available at <https://www.sec.gov/rules/other/2020/ic-33809.pdf> (“Release”).

<sup>3</sup> The \$22.8 trillion figure represents total net assets of mutual funds (including money market funds) and exchange-traded funds (ETFs) as of March 2020 as reported in ICI’s statistical releases Trends in Mutual Fund Investing March 2020 and Exchange-Traded Fund Report March 2020 and total net assets of closed-end funds and unit investment trusts as of December 2019 as reported in ICI’s forthcoming 2020 Investment Company Fact Book, p. 31. Mutual funds and ETFs comprised 98 percent of the assets in these funds at year-end 2019.

<sup>4</sup> 2020 Investment Company Fact Book (forthcoming) p. 31.

<sup>5</sup> 2020 Investment Company Fact Book (forthcoming) p. 33.

ETFs.<sup>6</sup>

Over the past two decades, not only have fund assets increased, but so have the variety of investment objectives and strategies funds pursue to meet the needs of investors who are seeking ways to save for their most important financial goals. ETFs are now a popular exchange-traded option, and funds of funds also have grown, providing a different way to access a strategy through a fund primarily investing in other funds. Target date and lifestyle funds (common types of funds of funds), emerging market and international funds, along with newer investment objectives like alternative strategy funds, have attracted strong flows. It is a diverse industry providing a variety of ways for investors to meet their financial goals.

## I. Executive Summary

The name of a fund is a tool for communicating with investors yet it is well recognized that no one should place too much reliance on a fund's name. Indeed, when the Names Rule was adopted, the Commission stated:

investors should not rely on an investment company's name as the sole source of information about a company's investments and risks.<sup>7</sup>

This is, and must remain, an important guiding principle as the Commission considers the framework for fund names. When the ICI and others seek to categorize funds, it is the investment objectives, strategies and portfolio holdings that inform the process, irrespective of a name.<sup>8</sup>

We believe that a second important principle for a fund names framework is to ensure that it is implemented in a manner consistent with Commission statements and rulemaking standards. As observed in the Release, prior to adoption of the Names Rule, the views of staff of the Division of Investment Management changed over time and were primarily expressed in staff guidelines and generic "Dear Registrant" letters.<sup>9</sup> Today, a similar process still is used through the disclosure review process, resulting in changing and differing staff comments to individual registrants and therefore different approaches across funds. This presents complexity and difficult challenges for Commission staff and funds as well as for investors.

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<sup>6</sup> 2020 Investment Company Fact Book (forthcoming) at 38. ICI's Fact Books are available at [https://www.ici.org/research/industry\\_research/fact\\_book](https://www.ici.org/research/industry_research/fact_book).

<sup>7</sup> Investment Company Names, SEC Release No. IC-24828 (Jan. 17, 2001), available at <https://www.sec.gov/rules/final/ic-24828.htm> ("Adopting Release").

<sup>8</sup> ICI seeks to categorize funds as objectively as possible by applying predetermined rules and definitions to the prospectus language of mutual funds, ETFs, and closed-end funds, with a special focus on the "Investment Objective" and "Principal Investment Strategies" sections. The proprietary Morningstar categories for funds focus on a fund's portfolio holdings. *See* Morningstar Investing Glossary: Morningstar Category, available at [https://www.morningstar.com/InvGlossary/morningstar\\_category.aspx](https://www.morningstar.com/InvGlossary/morningstar_category.aspx).

<sup>9</sup> Release at II.

In summary and consistent with these principles, we have the following recommendations for the Commission as it considers the framework for the Names Rule:

- We agree that funds today use derivatives in a variety of ways and that the asset-based testing approach of the Names Rule, often translated as implying a “market value” approach to valuing derivatives for Names Rule purposes, raises challenges for funds that gain investment exposure through derivatives. Rather than requiring funds to test all investments for Names Rule purposes using market value, or mandating certain valuation methods for specified derivative types, the Commission should permit funds to test each derivative type for Names Rule purposes consistent with a reasonable exposure metric and method that best measures the exposure the derivative obtains synthetically, which may or may not represent the cost or present value of the instrument.
- We recommend that the Commission not adopt a Names Rule test requiring that the type of investment suggested by a fund’s name contribute at least a minimum amount to a fund’s returns, as doing so could lead to less clarity and less certainty for fund investors.
- We recommend that the Names Rule’s current 80% threshold and approach continue to apply at the time of investment.
- We recommend that the Commission clarify that references such as “ESG,” “Sustainable,” “Responsible” or other names of funds with investment mandates requiring qualitative assessment of environmental, social or governance-related factors not be required to comply with the Names Rule, as these names suggest an investment strategy akin to names like “growth” or “value.”
- We recommend that the Commission reaffirm that the Names Rule does not apply to the terms “global” and “international” and that the Commission reaffirm that funds may “use any reasonable definition” of terms like “large-cap,” “mid-cap” or small-cap.”
- We recommend that the Names Rule not apply to fund ticker symbols, as investors should not be encouraged by Commission rule to expect to be able to rely on a single word or string of letters for any meaningful information about the fund’s investments and risks.
- We recommend that “tax-exempt” funds be permitted to have an 80% policy that may be changed without a shareholder vote so long as there is at least 60 days’ notice to shareholders, as permitted for other funds under the Names Rule.
- We encourage the Commission to explore ways to leverage technology to modernize disclosure and improve the effectiveness of disclosure for investors, including through hyperlinks, as well as in the delivery of disclosure, such as electronic delivery and notice and access.

## II. Application of The Names Rule's 80% Threshold

### A. *Asset-Based Testing and Use of Derivatives*

The Commission notes that the Names Rule has not been amended since its 2001 adoption despite significant changes in the fund industry, including with respect to funds' use of derivatives. Funds use derivatives in a variety of ways to achieve their investment objectives and as part of their investment strategies and policies. For example, funds use derivatives to obtain economic exposure to various markets, asset classes, issuers and indexes, often in cases where direct access is costly or difficult (if not impossible) to obtain. Funds also use derivatives to hedge exposures and manage risks, including interest rate risk and duration. In these ways, among others, derivatives provide important benefits for funds and their shareholders.

The Names Rule requires a fund to invest at least 80% of its assets in the investment suggested by its name. In this regard, the Commission acknowledges that asset-based testing may not be compatible with fund derivatives investments providing potentially significant exposures despite relatively small market values. As the Commission notes, funds may feel compelled to use a market value approach to valuing derivatives for Names Rule purposes in light of the Names Rule's asset-based test.<sup>10</sup> As a result, Names Rule compliance can be particularly challenging for funds that gain investment exposure through the use of derivatives. The Commission asks whether, in light of these challenges, an asset-based test is appropriate for determining whether a fund's name is misleading, and whether and how the Commission should address the Names Rule compliance challenges faced by funds investing in derivatives.

We agree that the asset-based approach is not well calibrated to funds' use of derivatives to obtain investment exposures that, in some cases, far exceed derivatives' market values. Permitting funds to test for Names Rule purposes using appropriate exposure metrics and methods, rather than requiring asset-based testing for all investments, would not only make the Names Rule more workable and economically realistic, it would also benefit shareholders by more closely aligning fund names with their true economic exposure. As we have previously commented to the Commission,<sup>11</sup> providing an alternative to asset-based testing, such as an exposure-based approach, best serves the Names Rule's purposes of providing investors "greater assurance that the company's investments will be consistent

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<sup>10</sup> See Release at text accompanying n.27 ("We understand that, although many funds have asserted that a derivative's notional value would be more appropriate than its market value for purposes of complying with the 80 percent investment policy, *funds generally use market value on account of the Names Rule's asset-based test.*") (emphasis added). Commission staff disclosure comments received by ICI members also suggest that a market value approach to valuing derivatives is to be used in all cases for Names Rule purposes.

<sup>11</sup> See Letter from Karrie McMillan, General Counsel, ICI, to Elizabeth M. Murphy, Secretary, SEC, dated November 7, 2011, available at <https://www.sec.gov/comments/s7-33-11/s73311-46.pdf> at n. 40 ("We believe that looking at the fund's exposure to the reference asset also best serves the purposes of rule 35d-1, the fund names rule.").

with its name” and “reduc[ing] confusion when an investor selects an investment company for specific investment needs and asset allocation goals.”<sup>12</sup>

The Commission has recognized that valuing derivatives using metrics other than market value can be appropriate for other compliance considerations. For example, in 2011, the Commission:

- sought comment on whether “a different measure of value than the statutory definition of ‘value’” would be appropriate for fund diversification testing;
- acknowledged that, for purposes of certain calculations under Rule 12d3-1 “the exposure of the fund to its counterparty or its exposure to the issuer of a reference security may be understated were the current market or fair value of the derivative the appropriate measure” and that “[t]he potential future exposure of the fund to the securities-related issuer is, in each case, likely to be unaccounted for by a current mark-to-market standard;” and
- inquired whether funds test for compliance with concentration requirements by “consider[ing] current market value or the notional amount of a derivative (or some other measure).”<sup>13</sup>

At the time, the Commission noted that funds’ use of derivatives “also may raise issues” under other Investment Company Act provisions, including Section 35(d) and Rule 35d-1.<sup>14</sup>

More recently, the Commission’s proposed Rule 18f-4 provided an exposure-based exception to the proposed requirements to adopt a derivatives risk management program and comply with a limit on fund leverage risk.<sup>15</sup> This proposed exposure-based exception would rely on the concept of “derivatives exposure,” defined under proposed Rule 18f-4 to mean “the sum of the notional amounts of a fund’s derivatives instruments and, for short sale borrowings, the value of any asset sold short.”<sup>16</sup>

These examples reflect the Commission’s understanding that, in some cases, a market value approach to valuing certain derivatives may divorce compliance testing from the economic reality faced by a fund invested in such derivatives. This concern is equally, if not more, significant when seeking to avoid deceptive or misleading fund names under Section 35(d). Rather than requiring funds to test all

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<sup>12</sup> See Adopting Release at I.

<sup>13</sup> See Use of Derivatives by Investment Companies under the Investment Company Act of 1940, SEC Release No. IC-29776 (Aug. 31, 2011), available at <https://www.sec.gov/rules/concept/2011/ic-29776.pdf>.

<sup>14</sup> See *id.* at n.16 and accompanying text.

<sup>15</sup> See Use of Derivatives by Registered Investment Companies and Business Development Companies; Required Due Diligence by Broker-Dealers and Registered Investment Advisers Regarding Retail Customers’ Transactions in Certain Leveraged/Inverse Investment Vehicles, SEC Release Nos. 34-87607, IA-5413, IC-33704 (Nov. 25, 2019), available at <https://www.sec.gov/rules/proposed/2019/34-87607.pdf>.

<sup>16</sup> See proposed Rule 18f-4(a). In determining “derivatives exposure,” the Commission would permit funds to adjust the notional amounts of interest-rate derivatives to a 10-year bond equivalent and delta adjust the notional amounts for options contracts.

investments for Names Rule purposes using market value, or mandating certain valuation methods for specified derivative types (which approach risks growing stale as investment products develop), the Commission should permit funds to test each derivative type for Names Rule purposes consistent with a reasonable exposure metric and method that best measures the exposure the derivative obtains synthetically, which may or may not represent the cost or present value of the instrument. Such an approach would be reasonable, would facilitate better alignment between Names Rule testing and the economic reality faced by a fund gaining investment exposure through derivatives, and would be consistent with other common approaches under the Names Rule.<sup>17</sup>

*B. Projected Return-Based Testing*

The Commission asks whether, instead of asset-based testing, the Commission should consider a Names Rule test requiring that the type of investment suggested by a fund's name contribute at least a minimum amount to a fund's returns. We believe that such a test would be unworkable and potentially misleading. While portfolio management decisions may involve projected returns, such projections are subject to numerous constraints and variables. Aggregating these projections across a fund's portfolio for Names Rule purposes would subject the fund's Names Rule compliance to the aggregated uncertainty of such projections, which could lead to less clarity and less certainty for fund investors.

*C. Time of Investment is the Appropriate Time for Application of the 80% Threshold*

The Commission asks whether the Names Rule's 80% threshold should continue to apply at the time of investment. There should be no change to this requirement of the Names Rule. All funds, including those subject to the Names Rule, remain, at all times, subject to Section 35(d)'s prohibition on "materially deceptive or misleading" fund names. It is important not to artificially constrain the investment flexibility of funds subject to the Names Rule, potentially to the detriment of fund shareholders, by expanding or changing the time of application of the 80% threshold. There is no need to attempt to duplicate the ongoing protections of Section 35(d)'s antifraud provisions by applying the 80% threshold differently.

The Commission recognized in the Names Rule Adopting Release that the 80% requirement was an "under normal circumstances" standard and accordingly provides funds with flexibility to manage their portfolios. The Commission stated that this standard permits funds "to take 'temporary defensive positions' to avoid losses in response to adverse market, economic, political, or other conditions." The Commission further noted that the standard permits funds "to depart from the 80% investment

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<sup>17</sup> For example, with respect to terms such as "small-cap," "mid-cap" and "large-cap," the Commission staff has stated that a fund using such a term in its name may use "any reasonable definition" for such term. See Frequently Asked Questions about Rule 35d-1 (Investment Company Names) ("Names Rule FAQs") at Question 6, available at <https://www.sec.gov/divisions/investment/guidance/rule35d-1faq.htm>. Likewise, the Commission staff has stated that a "fund that uses a name suggesting that its bond portfolio has a particular duration, e.g., short, intermediate, or long, may use any reasonable definition of the terms used." *Id.* at Question 12.

requirement in other limited, appropriate circumstances, particularly in the case of . . . large cash inflows or redemptions.”<sup>18</sup> This is very important to funds and their investors and should not be changed or disturbed. A continuous requirement to maintain compliance with the 80% threshold could result in a fund being forced to sell positions at inopportune times or to make investments solely for purposes of Names Rule compliance rather than consistent with what the portfolio manager believes to be in the best interest of fund shareholders. Fund shareholders’ interests are better protected by applying the Names Rule’s 80% threshold at the time of investment and under normal circumstances, relying on the ample protection from materially deceptive or misleading names afforded under Section 35(d) on an ongoing basis.<sup>19</sup>

As the Commission explained in proposing the Names Rule, the current time-of-investment approach is consistent with fund diversification testing under Section 5(c).<sup>20</sup> A host of other Investment Company Act provisions also apply tests at the time of investment,<sup>21</sup> and as noted above, in the Names

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<sup>18</sup> Adopting Release at II.A.4.

<sup>19</sup> A distinct approach was taken with respect to the 15% illiquid investment provisions of Rule 22e-4 under the Investment Company Act. Rule 22e-4 prohibits a fund from *acquiring* any illiquid investment if, *immediately after the acquisition*, the fund would have invested more than 15% of its net assets in illiquid investments that are assets, and the Commission noted its aversion to forcing sales of illiquid investments at deeply discounted prices for compliance purposes. *See* Investment Company Liquidity Risk Management Programs, SEC Release Nos. 33-10233, IC-32315 (Oct. 13, 2016), available at <https://www.sec.gov/rules/final/2016/33-10233.pdf> (“*requiring* a fund to divest illiquid investments if the fund’s holdings of illiquid investments that are assets exceed 15% of net assets . . . could result in the fund needing to sell the illiquid investments at prices that incorporate a significant discount to the investments’ stated value, or even at fire sale prices . . . [and] could adversely affect shareholders.”) (emphasis in original). However, the rule also contemplates bringing illiquid investments that are assets back into compliance with the 15% limit in a “reasonable period of time” in the event that the fund exceeds the limit. *See* Rule 22e-4(b)(1)(iv)(A) (requiring the liquidity program administrator to report to the fund’s board, among other things, “how the fund plans to bring its illiquid investments that are assets to or below 15% of its net assets within a reasonable period of time”) and (B) (requiring the fund’s board, including a majority of the independent directors, to “assess” whether the liquidity program administrator’s plan “continues to be in the best interest of the fund” in the event that the fund’s illiquid investments that are assets remain above 15% of net assets 30 days from the initial occurrence). Such an additional (and effectively ongoing) compliance requirement makes comparatively more sense in the context of a rule like Rule 22e-4, which is designed to assess and manage fund liquidity risk (the risk that the fund could not meet requests to redeem shares issued by the fund without significant dilution of remaining investors’ interests in the fund), than it would in the context of an anti-fraud rule like the Names Rule, which furthers the purposes of the anti-fraud provisions of Section 35(d).

<sup>20</sup> *See* Investment Company Names, SEC Release No. IC-22530 (Feb. 27, 1997), available at <https://www.sec.gov/rules/proposed/ic-22530.txt> (“Proposing Release”); see also Investment Company Act Section 5(c) (“A registered diversified company which at the time of its qualification as such meets the requirements of paragraph (1) of subsection (b) shall not lose its status as a diversified company because of any subsequent discrepancy between the value of its various investments and the requirements of said paragraph, so long as any such discrepancy existing immediately after its acquisition of any security or other property is neither wholly nor partly the result of such acquisition.”). The Commission also noted that applying the 80% threshold at the time of investment permits continued Names Rule compliance despite large cash inflows. *See* Proposing Release at n.28

<sup>21</sup> *See e.g.*, Section 12(d)(1)(H) (providing that, for purposes of Section 12(d)(1), “the value of an investment company’s total assets shall be computed *as of the time of a purchase or acquisition or as closely thereto as is reasonably possible*”); Rule 2a-7(d)(2) (“The money market fund must limit its portfolio investments to those United States dollar-denominated securities that *at the time of acquisition* are eligible securities.”); and Rule 12d3-1(b) (providing three conditions, each applied “*immediately after the acquisition*” or “*immediately after any such acquisition*,” under which, notwithstanding

Rule context, Section 35(d) sufficiently protects fund shareholders from materially deceptive or misleading names afforded on an ongoing basis.

III. Challenges in Assessing Whether or How the Names Rule Applies to Certain Fund Names

A. *The Commission Should Clarify that References such as “ESG,” “Clean,” “Environmental,” “Impact,” “Responsible,” “Social,” or “Sustainable” in Fund Names Reflect Types of Strategies and Not Types of Investments or Industries*

The Commission has made clear that “investors should not rely on an investment company’s name as the sole source of information about a company’s investments and risks” and that “[a]n investment company’s name, like any other single piece of information about an investment, cannot tell the whole story about the investment company.”<sup>22</sup> To this end, the Commission has made clear that certain terms in fund names do not trigger application of the Names Rule. Examples include terms in fund names “that connote types of investment strategies as opposed to types of investments,” such as “growth” and “value.”<sup>23</sup> The Commission staff has noted that each of “tax-sensitive” and “income” is an example of a term that “connotes a type of investment strategy rather than a focus on a particular type of investment.”<sup>24</sup>

The Commission notes that a growing number of funds disclose investment mandates requiring qualitative assessment of environmental, social or governance-oriented factors, and that such funds often reference these parameters in their names, using words or terms such as “ESG,” “Clean,” “Environmental,” “Impact,” “Responsible,” “Social,” “Sustainable” or “Sustainable Leaders” (fund names with such terms or phrases are referred to herein as “ESG Names,” and funds with ESG Names, “ESG Funds”). The Commission also notes that its staff has observed that some ESG Funds appear to consider such references in ESG Names to reflect an investment strategy and, thus not subject to the Names Rule’s 80% requirement, while other ESG Funds adopt such 80% policies.

We understand that the Commission staff has indicated through comments on registration statement disclosures that it expects any ESG Fund to adopt a policy to invest 80% of its assets in ESG-related investments defined using the criteria or process disclosed in the fund’s prospectus. We understand that many ESG Funds have disagreed with this staff position on the basis that the fund is pursuing a

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Section 12(d)(3), an acquiring company may acquire any security issued by a person that, in its most recent fiscal year, derived more than 15% of its gross revenues from securities related activities) (emphasis added in each case).

<sup>22</sup> Adopting Release at I.

<sup>23</sup> Adopting Release at II.C.1.

<sup>24</sup> See Names Rule FAQs at Questions 8 and 9.



particular investment strategy, similar to a “value” or “growth” investment strategy. As a result, some ESG Funds have implemented an 80% policy under the Names Rule, while others have not, meaning that disclosure varies among ESG Funds.

The Commission asks whether the Names Rule should apply to ESG Funds. Far from necessarily suggesting investment in certain investments or industries, or countries or geographic regions, or tax exempt investments, ESG Names suggest that fund strategies will be sensitive to and seek to align with the values or goals they reflect, which can vary significantly from fund to fund. ESG funds employ sustainable investing strategies, which use ESG analysis as a significant part of the fund’s investment thesis to seek to pursue investment returns and ESG-related outcomes. For example, a fund pursuing a sustainable investing strategy may screen for, or tilt towards, particular investments using ESG considerations. In other words, ESG Names suggest a type of strategy, much more akin to fund names incorporating terms like “growth,” “value,” “tax-sensitive” and “income” than to fund names incorporating terms like “stock” or “bond” that suggest a focus on a particular investment type. Similarly, the wide variety of ESG Funds and strategies they represent belies the notion that ESG Names indicate a focus in a particular industry.<sup>25</sup>

To insist that ESG Names suggest a particular type of investment or investment in a particular industry would be to ignore the variety of investment types, the rapid evolution of existing industries, and the creation of new industries, that are or would be appropriate investments for ESG Funds under their investment mandates. Requiring the adoption and implementation of a Names Rule-compliant 80% policy would, in the same way, artificially constrain ESG Funds and potentially prevent them from effectively implementing their investment mandates over time as investment types and industries evolve. It may also constrain or inhibit market-based efforts addressing disclosure considerations related to ESG Names and strategies. Several organizations and groups have undertaken efforts to define or categorize ESG investing terms, broadly seeking to improve investor understanding and mitigate concerns about investor confusion.<sup>26</sup>

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<sup>25</sup> See Adopting Release at II.A.1. ESG matters vary widely but are generally considered to include topics related to climate change, diversity and inclusion, human rights, the rights of company shareholders, and companies’ compensation structures. Investors are better served reviewing a fund’s investment objective and principal investing strategies than pinning their understanding of a fund’s strategy to its name.

<sup>26</sup> For example, the CFA Institute (“CFA”) has undertaken a project to develop an ESG industry standard that will establish minimum disclosure requirements for different ESG-related investment approaches. The CFA’s global industry standards team, which is responsible for the Global Investment Performance Standards (“GIPS”) and the CFA Institute Asset Manager Code, is leading the effort. The Institute of International Finance (“IIF”) also has done work in this area focusing on defining ESG investing terminology. IIF recently released a report that recommends simplifying sustainable investment terminology and product names into a few broad categories to align the industry around fewer, simpler sustainable investing terms. Similarly, the UK’s Investment Association (“IA”) recently launched a Responsible Investment Framework (the “Framework”) that defines and categorizes common approaches to “responsible investment.” The goal of the Framework is to establish a “common language” for how asset managers market responsible investment strategies to investors. The Framework establishes definitions for both fund-level and firm-level components of responsible investing.

Along with efforts to help investors better understand ESG with respect to funds and managers, we note there also are efforts related to specific ESG investments. For example, the International Capital Markets Association (“ICMA”) has

Consistent with this view, the Commission's Division of Corporation Finance Director William Hinman explained in a March 2019 speech the staff's view with respect to prescriptive requirements for operating company disclosures with respect to sustainability:

We hear differing views on whether disclosure requirements [concerning sustainability disclosures] should be principles-based or prescriptive, and whether they should utilize a specific set of reporting standards to enhance comparability.

So it appears to me that the market is still evaluating what, if any, additional disclosure on these topics would provide consistently material and useful information. The marketplace evolution of sustainability disclosures is ongoing . . . and allowing this evolution to continue should provide market participants with a continued opportunity to sort out the types of information they find useful. Had we leapt into action and issued prescriptive sustainability disclosure requirements when people first began calling for them, I believe we would have stymied that evolution and stifled efforts to develop useful disclosure frameworks. Substituting regulatory prescriptions for market-driven solutions, especially while those solutions are evolving, . . . is something we need to manage with utmost care.<sup>27</sup>

Of course, should a particular ESG Fund desire to adopt and implement an 80% investment policy voluntarily in a manner consistent with its ESG values or goals, it should be free to do so. But the Commission should make clear that the Names Rule does not mandate all ESG Funds to do so. Any such ESG Fund would remain subject to Section 35(d), and as noted above, because a fund's name "cannot tell the whole story about the investment company,"<sup>28</sup> it would be obligated to appropriately describe its investment strategies and risks in its summary, and full-length, prospectus. Moreover, as the Commission suggests in the Release, alternatives such as permitting funds to utilize hyperlinks and other innovative approaches to connect to more detailed discussions would further enhance investor understanding, both generally and particularly with regard to the nuanced and specific concepts that may be reflected in ESG Names.

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focused on ESG "assets" such as "green bonds," developing a set of voluntary guidelines, the Green Bond Principles, that provide issuers with guidance on the key components involved in the issuance of green bonds. The Green Bond Principles do not seek to define what green bonds are or set out comprehensively eligible categories of green bond projects. Rather, they recommend that issuers communicate clearly and transparently so that investors can make their decisions based on their determination of the bond's consistency with their investment strategy. ICMA also has principles for Social Bonds and guidance for Sustainability Bonds.

<sup>27</sup> See William Hinman, Director, Division of Corporation Finance, SEC, *Applying a Principles-Based Approach to Disclosing Complex, Uncertain and Evolving Risks: Remarks at the 18th Annual Institute on Securities Regulation in Europe* (Mar. 15, 2019), available at <https://www.sec.gov/news/speech/hinman-applying-principles-based-approach-disclosure-031519>.

<sup>28</sup> Adopting Release at I.

*B. Ongoing Challenges with Fund Names Suggesting Investments with a Geographic or Capitalization Focus*

**1. “Global” or “International” Funds**

The Commission notes that the Names Rule does not apply to the use of “global” or “international” in fund names and asks whether it should. The Commission should not, after nearly two decades, reverse its approach to the use of “global” or “international” in fund names by subjecting them to the Names Rule.

The Commission and its staff have acknowledged that prior prescriptive guidance on the use of “global” and “international” in fund names (indicating that the terms refer to investment in a specific minimum number of countries) has been rescinded.<sup>29</sup> As the Commission has acknowledged, “these terms may describe a number of investment companies that have significantly different investment portfolios” and “the number of countries in which [such a fund] may invest at any one time may appropriately differ from company to company.”<sup>30</sup> Funds have relied on this long-standing guidance and have adopted a variety of reasonable approaches to aligning investment strategies with fund names that use “global” or “international.” The Commission should confirm that any such reasonable approach is permissible so long as it is consistent with the antifraud protections of Section 35(d).

Moreover, as the use of “global” or “international” in a fund name is not subject to the Names Rule,<sup>31</sup> the Commission should reject efforts to impose a specific test or requirement for funds relating to the use of “global” or “international” in their names or to the way in which such funds determine whether a security is economically tied to a particular country. ICI members have expressed concern over Commission staff disclosure comments related to the use of these terms in fund names. Such comments have, for example, suggested prescriptive standards for the percentage of assets invested outside the United States and criticized approaches to determining whether a security is economically tied to a particular country. These efforts to impose through disclosure review specific tests related to the use of “global” or “international” in fund names or to the way in which such funds determine a security is economically tied to a particular country are inconsistent with the Commission’s approach

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<sup>29</sup> See Proposing Release at n.38 (“In the past, the Division distinguished ‘global’ and ‘international’ investment companies by suggesting that an investment company with ‘global’ in its name invest in securities of at least 3 different countries (which may include the United States) and that an investment company with ‘international’ in its name invest in securities of at least 3 countries outside the United States. . . . The Division no longer distinguishes the terms ‘global’ and ‘international.’”); Adopting Release at n.42 (citing Letter to Registrants from Carolyn B. Lewis, Assistant Director, Division of Investment Management, SEC (Jan. 3, 1991), noting that such letter was rescinded, and noting that “The terms ‘international’ and ‘global,’ however, connote diversification among investments in a number of different countries *throughout* the world, and ‘international’ and ‘global’ funds will not be subject to the rule. We would expect, however, that investment companies using these terms in their names will invest their assets in investments that are tied economically to a number of countries throughout the world.”); Names Rule FAQs at n.11 (citing Adopting Release at n.42).

<sup>30</sup> Proposing Release at II.C.1.

<sup>31</sup> Names Rule FAQs at Question 10 (“The terms ‘international’ and ‘global’ connote diversification among investments in a number of different countries *throughout* the world, and therefore the use of these terms in a fund name is not subject to the rule.”).

of not subjecting the use of these terms to the Names Rule. They also are particularly problematic in view of the extensive and varied ways in which industries and issuers have globalized and continue to evolve their locations, operations and work forces. The Commission should confirm that funds may utilize any reasonable approach to aligning investment strategies with fund names that use “global” or “international,” consistent with Section 35(d).

## 2. “Large-Cap,” “Mid-Cap” and “Small-Cap” Funds

ICI members have also expressed concern over Commission staff comments related to the use of terms such as “small-cap,” “mid-cap” and “large-cap” in fund names. Such comments reflect differing views on acceptable approaches to Names Rule compliance for funds with such terms in their names. For instance, in some cases Commission staff has objected to particular dollar ranges used to identify particular categories of capitalization, or to defining a capitalization category by reference to an industry index for that capitalization category. The Commission should reaffirm the Commission staff’s longstanding guidance that “an investment company may use any reasonable definition of these [capitalization-related] terms”<sup>32</sup> and acknowledge the adequacy of Section 35(d)’s antifraud protections in this context.

### C. *Ticker Symbols*

The Commission asks whether the Names Rule should apply to fund ticker symbols. It should not. Even where a ticker symbol may be selected in part because of some general reference to the fund’s investment strategies, it is an even briefer, less explanatory piece of information than the fund’s name. As noted above, the Commission has stated that “investors should not rely on an investment company’s name as the sole source of information about a company’s investments and risks.”<sup>33</sup> This is even truer with respect to a fund’s ticker symbol, which is at best a single word and may be no more than a string of letters. A Commission rule should not encourage investors to expect to be able to rely on this single word or string of letters for any meaningful information about the fund’s investments and risks.

## IV. Other Ways the Commission Could Improve the Names Rule and Provide Better Information to Investors

The Commission requests comment on ways that the Names Rule should be modified to provide greater investment flexibility while still requiring that fund names suggesting a certain focus effectively convey the nature of a fund’s investments, and on whether there are alternative ways to regulate or address fund names that would more effectively protect investors. One such improvement would be for the Commission to harmonize the Names Rule requirements for tax-exempt funds with those of other funds subject to the Names Rule. Other improvements would be to permit the use of hyperlinks and

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<sup>32</sup> See *id.* at Question 6. The Commission staff’s guidance provides that “pertinent references” may include “industry indices, classifications used by mutual fund rating organizations, and definitions used in financial publications.” *Id.*

<sup>33</sup> Adopting Release at I.

other technologies in addressing Section 35(d) concerns and taking steps to modernize the shareholder notice requirements of the Names Rule.

**A. *Harmonizing Certain Names Rule Requirements for Tax-Exempt Funds and Other Funds Subject to the Names Rule***

In adopting the Names Rule, the Commission bifurcated the proposed requirement that all funds subject to the Names Rule adopt an 80% policy that is a fundamental policy that may not be changed without shareholder approval. For funds with names suggesting investment in certain investments or industries, or funds with names suggesting investment in certain countries or geographic regions, the Commission provided the option of adopting an 80% policy that is fundamental or, alternatively, an 80% policy that may be changed without shareholder approval so long as there is at least 60 days' notice provided to shareholders, where the notice meets certain specifications. On the other hand, the Commission adopted the requirement that tax-exempt funds adopt 80% policies as fundamental. The Commission explained this distinction by reference to the "critical importance of the tax-exempt status" to such funds' investors.<sup>34</sup>

While the ICI and its members agree that a fund's tax-exempt status is important to such funds' investors, it is unclear why this fact warrants such a distinct approach to Names Rule compliance. The Commission explained that, for a non-tax exempt fund subject to the Names Rule, shareholders "will have sufficient time to decide whether to redeem their shares in the event that the investment company decides to pursue a different investment policy."<sup>35</sup> The same would be true of tax-exempt fund investors if tax-exempt funds were accorded the same flexibility to adopt either a fundamental 80% policy or an 80% policy that may be changed without shareholder approval so long as there is at least 60 days' notice provided to shareholders.

**B. *Encouraging the Use of Hyperlinks and Other Technologies to Address Section 35(d) Concerns and Modernize Disclosure Delivery and Notice Requirements***

Terms in a fund's name like "balanced" fund, "growth" fund, or "target date" fund do not, and should not be expected to, explain to investors all they need to know about a fund. Similarly, recognizing that a fund's name is not the "sole source of information" about the fund's investments and risks, there are important ways and opportunities to improve disclosure. For example, there have been notable efforts to make target date fund disclosure more effective and useful for investors such as through the use of asset allocation glide path illustrations.<sup>36</sup>

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<sup>34</sup> See Adopting Release at II.A.1.

<sup>35</sup> See *id.*

<sup>36</sup> See, e.g., ICI Target Date Fund Disclosure Working Group, Principals to Enhance Understanding of Target Date Funds, June 18, 2009, available at [https://www.ici.org/pdf/ppr\\_09\\_principles.pdf](https://www.ici.org/pdf/ppr_09_principles.pdf). The Commission proposed amendments to certain fund advertising rules, but not the Names Rule, to require illustrations related to a fund's asset allocation over time. See Investment Company Advertising: Target Date Retirement Fund Names and Marketing, SEC Release Nos. 33-9126,

Consistent with this approach, the Commission should encourage funds to complement traditional investment strategy and risk disclosures with additional, detailed disclosures available and delivered to investors through a variety of approaches. For example, the Commission could encourage funds to hyperlink in electronic-based disclosure from abbreviated explanations to fuller, user-friendly and engaging descriptions of fund strategies and risks.<sup>37</sup>

As the Commission considers how technology could be used to foster investor understanding, we also strongly recommend that the Commission consider not only electronic disclosure but also facilitating electronic delivery of disclosure.<sup>38</sup> Recent events related to COVID-19, such as concerns about the delivery and receipt of physical mailings, reinforce the many benefits of electronic delivery of disclosures. Additionally, the specific notice requirements under Rule 35d-1(c) could be improved and “modernized” by removing the specific requirements relating to placement, font and wording of a particular statement to be included in the shareholder notice or on the envelope in which it is delivered.<sup>39</sup>

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We appreciate the opportunity to provide comments on the framework for addressing names of registered investment companies and business development companies that are likely to mislead investors about a fund’s investments and risks. If you have any questions, please contact me at (202) 326-5813 or Dorothy M. Donohue, Deputy General Counsel – Securities Regulation, at (202) 218-

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34-62300, IC-29301 (June 16, 2010), available at <https://www.sec.gov/rules/proposed/2010/33-9126.pdf>; Investment Company Advertising: Target Date Retirement Fund Names and Marketing, SEC Release Nos. 33-9570, 34-71861, IC-31004 (Apr. 3, 2014), available at <https://www.sec.gov/rules/proposed/2014/33-9570.pdf> (reopening comment period).

<sup>37</sup> See e.g., Request for Comment on Fund Retail Investor Experience and Disclosure, SEC Release Nos. 33-10503, 34-83376, IC-33113 (June 5, 2018), available at <https://www.sec.gov/rules/other/2018/33-10503.pdf> (“A modern fund disclosure system should provide investors streamlined and user-friendly information that is material to an investment decision, while providing them the ability to access additional, more in-depth information on-demand. We developed our current disclosure requirements at a time when investors received information primarily on paper. Some have criticized fund prospectuses and other required disclosure documents for containing long narratives; generic, redundant, and even at times irrelevant disclosures; legalese; and extensive disclosure that may serve more to protect funds from liability rather than to inform investors. As technology evolves, the Commission seeks to improve the fund disclosure system to reflect the way investors currently seek, receive, view, and digest information. Advances in technology have made available new, innovative, and effective ways to improve the delivery, design, and content of fund disclosures. Electronic-based disclosures allow for more interactive, user-friendly design features tailored to meet individual investors’ needs and improve investor engagement.”).

<sup>38</sup> The Commission recently modernized delivery of shareholder reports, permitting funds to use notice and access. See Optional Internet Availability of Investment Company Shareholder Reports, SEC Release Nos. 33-10506, 34-83380, IC-33115 (June 5, 2018), available at <https://www.sec.gov/rules/final/2018/33-10506.pdf> (adopting 1940 Act Rule 30e-3); The Commission should continue its modernization efforts by reexamining its outdated framework for the use of electronic delivery more broadly. See Use of Electronic Media, SEC Release Nos. 33-7856, 34-42728, IC-24426 (Apr. 28, 2000), available at <https://www.sec.gov/rules/interp/34-42728.htm>.

<sup>39</sup> See Rule 35d-1(c)(2)-(3).

Ms. Vanessa Countryman

May 5, 2020

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3563, or our counsel, Corey F. Rose at (202) 261-3314, or Aaron D. Withrow at (202) 261-3442, at Dechert LLP.

Sincerely,

/s/ Susan M. Olson

Susan M. Olson  
General Counsel

cc: The Honorable Jay Clayton  
The Honorable Hester M. Peirce  
The Honorable Elad L. Roisman  
The Honorable Allison Herren Lee

Dalia O. Blass  
Director, Division of Investment Management