

[Securities Regulation Daily Wrap Up, TOP STORY—SEC okays reporting modernization, liquidity management and swing-pricing changes, \(Oct. 13, 2016\)](#)

Securities Regulation Daily Wrap Up

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By [Amy Leisinger, J.D.](#)

The SEC has approved three sets of final rules and form amendments affecting investment companies' reporting and operations. The Commission unanimously authorized changes to require mutual funds and other open-end management investment companies to adopt liquidity risk management programs, but, in the [meeting](#), Commissioner Michael Piwowar declined to support a rule permitting funds to use swing pricing in connection with redemptions and also voted against changes to modernize investing company reporting, citing the removal of a provision to allow for implied consent for electronic delivery of shareholder reports.

"These new rules represent a sweeping change for the industry by requiring strong transparency provisions and enhanced investor protections," [said](#) SEC Chair Mary Jo White. "Funds will more effectively manage liquidity risk and both Commission staff and investors will receive additional and better quality information about fund holdings."

Liquidity risk management. The Commission [approved](#) Rule 22e-4 to require open-end management investment companies, including ETFs, to adopt board-approved liquidity risk management programs that include classifications of the liquidity of portfolio assets and to conduct periodic evaluations of liquidity risk. The final rule provides four liquidity time-frame categories and requires reporting of the percentage of each classification on a quarterly basis on Form N-PORT. The changes also codify the current 15-percent limit on illiquid assets and require enhanced disclosure regarding fund liquidity and redemption practices. Funds must also now periodically review whether assets have become illiquid over time rather than making the determination only once at acquisition and use new Form N-LIQUID to confidentially notify the Commission when they exceed the illiquidity limitation or fall below their respective minimums with regard to highly liquid investments.

The rule excludes money market funds from all requirements and exchange-traded funds that qualify as "in-kind ETFs" from certain requirements. Most funds would be required to comply with the program requirements by December 1, 2018, while fund complexes with less than a \$1 billion in assets would be required to do so by June 1, 2019.

Swing pricing. With the [swing-pricing changes](#), open-end funds (other than money market funds or ETFs) would be permitted to pass the costs of trading activity to purchasing or redeeming shareholders through adjustments to net asset value to protect existing shareholders from associated dilution of shares. The swing factor would be included in a fund's net asset value once the level of net purchases or net redemptions exceeded a specified percentage, and swing-pricing policies and procedures would be subject to approval by each fund's board. Amendments to Form N-1A and Regulation S-X address financial-statement and performance reporting related to swing pricing and require funds that use the method to provide explanations in their respective registration statements.

Chair White [applauded](#) the change as another tool for funds to use in mitigating dilution and managing liquidity, noting the two-percent upper limit on a fund's use of swing pricing. Commissioner Kara Stein [agreed](#) that swing-pricing provides an effective method for allocating costs to the shareholders doing the buying and the selling but urged the staff and fellow commissioners to monitor funds' swing-pricing activities to ensure the rule does not lead to abusive pricing activities. In connection with such monitoring, the effective date of the rule will be delayed

for two years. Commission Piovolar [said](#), however, the limitations included in the rule are insufficient to protect investors and to prevent the potential for gaming prices for the benefit of large stakeholders.

Reporting modernization. The [reporting modernization rules](#) will enhance data reporting by registered investment companies and increase access, and the quality of, information available to the Commission and investors. The changes require funds to file new monthly portfolio reports with portfolio-wide and position-level holdings data on Form N-PORT and rescind Form N-Q on which funds currently report holdings for the first and third fiscal quarters. The information contained in reports for the last month of each fund's fiscal quarter would be publicly available after 60 days. New annual reporting form, Form N-CEN, would require registered funds to annually report certain census-type information and replace Form N-SAR. The form is designed to streamline and update reported information and will be filed annually within 75 days of the end of a fund's fiscal year. The information will be reported in a structured data format designed to allow for clearer analyses of, and comparisons among, companies. The rules also impose enhanced, standardized financial-statement disclosures and mandate disclosure relating to securities lending activities.

Most funds will begin filing reports on new Forms N-PORT and N-CEN after June 1, 2018. Fund complexes with less than a \$1 billion in net assets would begin filing reports on Form N-PORT after June 1, 2019.

Chair White and Commissioner Stein [noted](#) that most of the investment-company reporting rules have not been updated in many years and that the proposed enhancements will fill existing data gaps. According to Stein, additional information about holdings and operational risk measures will help the SEC and its staff to follow trends and better understand data being reported. Commission Piovolar voted against the measure, taking issue with the decision to delay consideration of Rule 30e-3. As [proposed](#), this rule would permit electronic transmission of a shareholder report if a fund provides a statement notifying the shareholder of its intent to make future reports available on its website until the shareholder revokes consent. This change promised a reduction in costs and now the benefit to shareholders has been indefinitely delayed, he said.

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