

SEC Releases New Guidance on Tailored Shareholder Reports

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On January 19, 2024, the Division of Investment Management staff at the Securities and Exchange Commission (SEC), released several responses to frequently asked questions (FAQs) related to the adoption of rules and form amendments for registered open-end funds (*i.e.*, mutual funds and ETFs) that will substantially alter the form and content of fund shareholder reports. In October 2022, the SEC [adopted amendments](#) (Adopting Release) to rules under the Securities Act of 1933 and Investment Company Act of 1940, as well as Forms N-1A and N-CSR, in an effort to require funds to, among other things, transmit “concise and visually engaging” shareholder reports.

The FAQs address what an appropriate broad-based securities market index is, Form N-CSR and website availability requirements, binding individual shareholder reports of multiple funds, electronically provided shareholder reports, and compliance date and Inline XBRL issues. The full text of the new FAQs can be found here: <https://www.sec.gov/investment/tailored-shareholder-reports-faqs>.

APPROPRIATE BROAD-BASED SECURITIES MARKET INDEX

- The final rules require a fund to show its performance against an “appropriate broad-based securities market index,” which is defined as “the overall applicable domestic or international equity or debt markets, as appropriate.” In the Adopting Release, the SEC stated that a fund must select an index that “reasonably represents” the applicable market, and provided examples that pertain to funds that invest primarily in equity securities, which left open questions for funds that primarily invest in fixed income securities.
- The staff clarifies that a fund that invests primarily in tax-exempt municipal securities, including a fund that invests primarily in the municipal income securities of a single state, may use an index that reflects the national **municipal** securities market as its appropriate broad-based securities market index, rather than an index that reflects the national **aggregate** fixed income securities market (emphasis added). The staff stated that, in their view, because tax-exempt municipal bonds are distinct from other types of securities, the national municipal securities market may be understood as a standalone overall market as opposed to a mere subset of the fixed income market. (FAQ #2)
- The staff’s omission of a FAQ related to other types of funds that invest primarily in fixed income securities (*e.g.*, high yield bond funds) may draw the negative implication that such funds do *not* warrant the special consideration seemingly paid to municipal fixed income funds, and, accordingly, may not use an index that reflects their related national fixed income securities market (*e.g.*, the national high yield bond market).

Accordingly, absent further guidance, a prudent approach for fixed income funds (other than tax-exempt municipal securities funds) would be to select an index that reflects the national aggregate fixed income securities market.

FORM N-CSR AND WEBSITE AVAILABILITY REQUIREMENTS

- In connection with each shareholder report, the final rules (rule 30e-1) require a fund to make certain disclosures required by Form N-CSR (Items 7 through 11) publicly available, free of charge, on the fund's website. Alternatively, the fund may post the complete Form N-CSR. For funds that are registered under the Investment Company Act of 1940, as amended (1940 Act), but that offer and sell their securities without registration under the Securities Act of 1933, as amended (Securities Act), the new regulatory requirement to disclose fund information raised questions regarding whether such disclosure would violate the prohibition on general solicitation and advertising in Regulation D under the 1933 Act.
- The staff clarifies that compliance with the requirement to post Form N-CSR information online under amended rule 30e-1 would not be a violation of rule 502(c) of Regulation D, so long as the fund posts only the information required by the rule and does not use its website to offer or sell securities or in a manner that is deemed to be general solicitation or advertising for offers or sales of its securities. (FAQ #5)

BINDING INDIVIDUAL SHAREHOLDER REPORTS OF MULTIPLE FUNDS

- New Instruction 4 to Item 27A(a) provides that a fund must prepare a separate shareholder report for each series of a fund, and if a series has multiple classes, to prepare a separate shareholder report for each class within the series. In the Adopting Release, the SEC stated that such requirement is intended to address circumstances where (1) one shareholder report addresses multiple funds and/or share classes; and/or (2) an investor receives information about multiple funds, but the investor is not actually invested in all of these funds.
- The staff clarifies that where an investor has invested in multiple funds (or in multiple share classes of funds), the individual shareholder reports of each of such funds (or, as applicable, share classes) may be bound, stapled, or stitched together for transmission to the investor because such practice does not raise the same concerns about multiseries shareholder reports that the SEC discussed in the Adopting Release. The staff notes that a fund should consider including a table of contents to any bound, stapled, or stitched shareholder report for investors' ease of use. (FAQ #6)

ELECTRONICALLY PROVIDED SHAREHOLDER REPORTS

- In FAQ #9, the staff clarifies that there is more than one approach that would be consistent with the requirements of Instruction 4 to Item 27A(a) of Form N-1A for a fund to deliver their fund and share-class specific shareholder report directly to an investor, including delivering an email, or otherwise electronically transmitting a notification to investors, that (i) includes direct links to the shareholder report(s) of the fund(s) and share class(es) that the investor owns, and (ii) specifies the investor's fund(s) and share-class(es) and includes a link directing the investor to a website landing page that includes direct links that are limited to the shareholder report(s) for the fund(s) and share class(es) that the investor owns. (FAQ #9)

COMPLIANCE DATE AND INLINE XBRL ISSUES

- In FAQ #10, the staff clarifies that funds should include the shareholder report that was actually transmitted to shareholders in the respective Form N-CSR, regardless of whether the Form N-CSR is filed before or after the compliance date, *i.e.*, July 24, 2024. (FAQ #10)

We are available to discuss these updates and other considerations related to the new Tailored Shareholder Reports requirements. Please do not hesitate to contact us with any questions.

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