

# SEC Adopts Amendments to ‘Names Rule’ Impacting Regulated Investment Funds

October 10, 2023

On September 20, the Securities and Exchange Commission (SEC), [adopted amendments](#) (Amendments) to [Rule 35d-1](#) (Names Rule) under the Investment Company Act of 1940, as amended (Investment Company Act). The Names Rule generally requires a registered investment company (RIC) or a business development company (BDC and collectively with a RIC, a “Fund” or “Funds,” as applicable) to invest at least 80 percent of the value of its assets in the particular type of investments, or in investments in the particular industry or industries, suggested by the Fund’s name. In its adopting release, the SEC noted that investors continue to consider environmental, social, and governance (ESG) factors when deciding where to allocate their capital, leading some Funds to exaggerate their ESG practices or the extent to which their investment products take into account ESG factors. Thus, as noted in the adopting release, the Amendments aim to promote transparency and accountability.

The Amendments expand the applicability of the Names Rule and require impacted Funds to implement an 80 percent Investment Policy (as defined below). Consequently, Funds may need to modify their names or alter their investment strategies to comply with the Amendments – potentially impacting their portfolios. The Amendments include, among other things, (i) the expansion of the types of names suggesting an investment focus; (ii) the ability for Funds to temporarily deviate from their 80 percent Investment Policy and to regain compliance as soon as practical but no later than 90 days; (iii) requirements to disclose quarterly if a Fund is not in compliance with the 80 percent Investment Policy; (iv) a requirement that a change to an unlisted Fund’s 80 percent Investment Policy generally requires shareholder approval with a few exceptions; and (v) guidance with respect to the use of derivative instruments when assessing the Fund’s adherence to its 80 percent Investment Policy.<sup>1</sup>

## Background

The Names Rule generally prohibits a Fund from adopting a name or part thereof that the SEC finds is materially deceptive or misleading. The SEC adopted the Names Rule back in 2001. The Names Rule requires that if a Fund’s name suggests that the Fund invests in a particular type of investment or investments, or in investments in a particular industry, group of industries, countries, or regions, then such Fund must adopt a policy to invest at least 80 percent of the value of its assets<sup>2</sup> in such industry, type of investment, or geographic region (an 80 percent Investment Policy).

## What’s Required by the Amendments?

The following is a summary of the key components of the Amendments:

### A. Names Suggesting Investment Focus

The Amendments expand the Names Rule’s 80 percent Investment Policy requirement beyond its current scope to apply to any Fund name with terms suggesting that the Fund focuses on investments that have, or investments whose issuers have, “particular characteristics.” The SEC did

<sup>1</sup> See SEC Fact Sheet available [here](#); see also SEC Press Release available [here](#).

<sup>2</sup> “Assets” means net assets, plus the amount of any borrowings for investment purposes.

not clearly define “particular characteristics,” but they did provide a few examples of terms that have “particular characteristics,” such as “growth,” “ESG” terms, “thematic” investment focus and “value.” Funds retain the flexibility to ascribe reasonable definitions for the terms used in a Fund’s name and to determine the specific criteria the Fund uses to select the investments that the term describes. However, as the SEC noted, “there must be a meaningful nexus between the given investment and the investment focus suggested by the name.” The SEC further mentioned that certain terms (e.g., “real return,” “balanced,” “managed risk,” “hedged,” “global or “international” on its own, and “long/short”) do not communicate to investors the “particular characteristics” of investments that will make up the Fund’s portfolio and as such, are not required to have an 80 percent Investment Policy. However, Funds with these names will continue to be subject to the prohibitions of Section 35(d) of the Investment Company Act and the general anti-fraud provisions of the federal securities laws regarding disclosures to investors even if a Fund adopts and implements an 80 percent Investment Policy.

## **B. Companies May Temporarily Depart From the Fund’s 80 Percent Investment Policy**

The Names Rule, in general, requires a Fund to invest in accordance with its 80 percent Investment Policy “under normal circumstances” and for the 80 percent investment requirement to apply at the time a Fund invests its assets. However, the Amendments (i) require a Fund to review its portfolio assets in its “80 percent basket” at least quarterly and (ii) allow Funds to deviate from the 80 percent requirement as a result of drift or other-than-normal circumstances and regain compliance within 90 days. Other-than-normal circumstances generally include, but are not limited to, market fluctuations, index rebalancing, cash flows/inflows or temporary defensive positions. Moreover, the Amendments allow newly formed Funds 180 days to comply with the 80 percent Investment Policy requirement because they may need a longer time to ramp up the portfolio and may be focused on investing in securities with a limited supply. The Amendments also do not specifically limit the length of time that a Fund may depart from the 80 percent Investment Policy requirement in the event of such Fund’s reorganization.

## **C. N-PORT Reporting, Recordkeeping, Notice Requirements and Prospectus Disclosure**

Pursuant to the Amendments, RICs (excluding money market funds and small business investment companies) that are required to have an 80 percent Investment Policy will now need to disclose on Form N-PORT whether each investment falls into the Fund’s “80 percent basket” and indicate the value of the “80 percent basket” as a percentage of the Fund’s total assets. Funds will have to report this information for the third month of every quarter. Therefore, any violation of an 80 percent Investment Policy by a Fund will be publicly available and easily noticeable.

The new recordkeeping requirement will require Funds with an 80 percent Investment Policy to document ongoing compliance with the amended Names Rule and maintain such records for six years. The Amendments also retain the concept from the current Names Rule that Funds must provide 60 days’ prior notice to shareholders of any change in its 80 percent Investment Policy unless the 80 percent Investment Policy is a fundamental policy (in which case shareholder approval would be required to amend the policy). The Amendments also require that the notice to shareholders describe (i) the nature of the change to the 80 percent Investment Policy, (ii) the Fund’s old and new names, and (iii) the effective date of any investment policy and/or name changes.

In regards to the prospectus disclosure, the final Amendments modify Forms N-1A and Form N-2, imposing additional disclosure requirements for Funds that are required to have an 80 percent Investment Policy by mandating such Funds to disclose and define the terms used in a

---

<sup>3</sup> Funds must tag most of the new information that will be included in a prospectus pursuant to the Amendments using a structured data language, specifically, Inline XBRL.

Fund's name inside of its prospectus.<sup>4</sup> If terms used in the Fund's name suggest a tax-exempt or particular investment focus, then the definition of such terms in the Fund's prospectus should be consistent with the plain English meaning of such terms or, conversely, as such terms are used and established by the industry that is the subject of the Fund's particular investment focus.

#### **D. Unlisted Closed-Ended Funds and BDCs**

Given the recent growth of unlisted Funds, the Amendments prevent a Fund whose shares are not listed on a national securities exchange that has an 80 percent Investment Policy from changing such policy without shareholder approval. However, the Amendments permit such Funds to change the 80 percent Investment Policy without a shareholder vote if: (1) the Fund conducts a tender or repurchase offer with at least 60 days' prior notice of the policy change, (2) that offer is not oversubscribed, and (3) the Fund purchases shares at their net asset value. As described in the adopting release, due to the generally illiquid nature of the shares held by investors in an unlisted Fund, the SEC believes that by conducting a tender offer or repurchase with 60 days' prior notice, investors in an unlisted Fund will have an opportunity to liquidate their shares in the Fund, if they disagree with the Fund's proposed change in the 80 percent Investment Policy. However, if a tender or repurchase offer is oversubscribed, a Fund would then be required to conduct a shareholder vote prior to making the change to its 80 percent Investment Policy.

#### **E. Derivatives and Valuation of Derivative Instruments**

The Amendments also aim to address the valuation of derivative instruments for purposes of determining a Fund's compliance with its 80 percent Investment Policy, as well as clarifying the types of derivatives that can be included in a Fund's "80 percent basket." The Amendments generally require that Funds holding derivative instruments use the notional amount (rather than the market value) of such instruments when assessing the Fund's adherence to its 80 percent Investment Policy. In addition, the Amendments require Funds to exclude from the "80 percent basket" certain derivatives that hedge currency risk with a Fund's foreign currency-denominated investment. Furthermore, the Amendments allow Funds to (i) deduct cash and cash equivalents and US Treasury securities with remaining maturities of one year or less from assets up to the notional amount of the derivative instrument when determining compliance with the 80 percent Investment Policy and (ii) exclude any closed-out derivatives positions when calculating assets for purposes of determining compliance with a Fund's 80 percent Investment Policy, if those positions result in no credit or market exposure to such Fund. The adopting release provides greater clarity with respect to the Names Rule to Funds that utilize derivatives – an area that traditionally lacked SEC guidance.

### **Integration Funds**

The SEC did not adopt a portion of the [proposed rules](#) in the Amendments that would have deemed an integration fund's (i.e., a fund that integrates ESG alongside non-ESG factors) name materially misleading if it included ESG terminology in its name. However, the SEC will continue to consider comments on this issue.

### **Compliance Dates**

The Amendments will become effective 60 days after publication in the Federal Register (the "Effective Date"). The compliance start date is 24 months following the Effective Date for Larger Entities and 30 months following the Effective Date for Smaller Entities.<sup>5</sup>

<sup>4</sup> Requires a majority approval by the outstanding voting securities of such Fund.

<sup>5</sup> "Larger Entities" are funds that, together with other investment companies in the same "group of related investment companies" (as such term is defined in rule 0-10 under the Investment Company Act) have net assets of \$1 billion or more as of the end of the most recent fiscal year.

"Smaller Entities" are funds that together with other investment companies in the same "group of related investment companies" have net assets of less than \$1 billion as of the end of the most recent fiscal year.

## Conclusion

According to the SEC’s adopting release, the Amendments are designed to help investors better understand how a Fund’s investment strategy corresponds with the investment focus that the Fund’s name suggests, as well as to provide additional information about how the Fund’s management seeks to achieve the Fund’s objective. As Commissioner Mark T. Uyeda [noted](#), the Amendments will create higher initial and ongoing costs by forcing Funds to define terms that are used in the Fund’s name in their prospectus disclosures and comply with the new Form N-PORT’s disclosure requirements and the Name Rule’s recordkeeping requirements. Existing Funds with a current 80 percent Investment Policy and with names containing such terms as “growth,” “value,” or “ESG” traits should examine their current names and portfolios to determine if they need to make definitional edits, change their name, and/or modify their investment focus or strategy. In addition, existing Funds without an 80 percent Investment Policy and new Funds that are in the process of being formed should review their current or proposed Fund names to determine if they will now be subject to the Names Rule as a result of the Amendments and assess whether they need to adopt an 80 percent Investment Policy or consider changing the name of the Fund. Funds should also review their Investment Company Act compliance policies and procedures and consider whether the Amendments necessitate any changes to such Fund’s policies and procedures.

---

## CONTACTS

For more information on how to comply with the Amendments, contact your Katten attorney or any of the following:



**Vlad M. Bulkin**  
+1.202.625.3838  
vlad.bulkin@katten.com



**Richard D. Marshall**  
+1.212.940.8765  
richard.marshall@katten.com



**Brandon A. Bucio**  
+1.469.627.7026  
brandon.bucio@katten.com

# Katten

katten.com

CENTURY CITY | CHARLOTTE | CHICAGO | DALLAS | LONDON | LOS ANGELES | NEW YORK | ORANGE COUNTY | SHANGHAI | WASHINGTON, DC

Attorney advertising. Published as a source of information only. The material contained herein is not to be construed as legal advice or opinion.

©2023 Katten Muchin Rosenman LLP. All rights reserved.

Katten refers to Katten Muchin Rosenman LLP and the affiliated partnership as explained at [kattenlaw.com/disclaimer](http://kattenlaw.com/disclaimer).

10/6/23