

Modernization of the SEC’s Reporting Requirements: What Investment Companies Should Know

By *Diana E. McCarthy and Benjamin D. McCulloch*

The Securities and Exchange Commission (SEC) has adopted new rules and forms, including amendments to existing rules and forms, to modernize and enhance disclosure for investment companies (the “Modernization Rules”).^[1] The Modernization Rules are the SEC’s response to the increasingly new and complex investment products and strategies used by investment companies. They pose significantly increased reporting obligations for funds.

The SEC set out to accomplish three goals through the Modernization Rules: (i) enhance the transparency of investment company portfolios and investment practices, both to the SEC and to investors; (ii) take advantage of technological advances in reporting of information to the SEC and in providing information to existing and potential investors; and (iii) reduce duplicative or unnecessary reporting burdens. Accordingly, the SEC made three key changes to the investment company reporting regime: (i) adopted Form N-PORT and rescinded Form N-Q; (ii) adopted Form N-CEN and rescinded Form N-SAR; and (iii) amended Regulation S-X to enhance and standardize current disclosure and increase the disclosure of derivatives and securities lending activities.

Forms N-PORT and N-CEN will be made publically available in data format. Though Form N-Port will be filed by funds on a monthly basis, only the fiscal quarter-end reports will be made publically available 60 days after the end of the fiscal quarter. Form N-CEN will be filed annually (75 days after fiscal year-end (for management companies) and calendar year-end (for UITs) and made publically available upon filing.

Form N-PORT

The SEC has rescinded Form N-Q and adopted a new portfolio reporting form, Form N-PORT, which requires all registered investment companies (other than money market funds and small business investment companies (SBICs) and unit investment trusts (UITs) that operate as exchange-traded funds, to report portfolio information in Extensible Markup Language format. Reports on Form N-PORT will be filed with the SEC separately for each series of a fund company on a monthly basis (no later than 30 days after the end of each month).

The adoption of Form N-PORT represents a significant increase in the volume of reporting obligations for investment companies. Under the previous regime, Form N-Q generally limited fund-specific disclosure to its schedule of investments as of the close of the reporting period. Reports on Form N-PORT will include

significantly more descriptive information in addition to the schedule of investments. In particular, Form N-PORT requires new disclosure of: (i) derivative investments; (ii) certain risk metric calculations that measure a fund’s exposure and sensitivity to changes in market conditions, such as changes in asset prices, interest rates or credit spreads; (iii) the fund’s monthly returns; (iv) net realized gains or losses and net change in unrealized appreciation or depreciation for the fund on its derivative and non-derivative investments, respectively; and (v) certain fund activities, such as securities lending, repurchase agreements and reverse repurchase agreements, including information about the counterparties.

Form N-PORT in a Nutshell

- Monthly filings, with every third report (fiscal quarter) made public 60 days after filing
- Replaces Form N-Q
- New disclosure requirements, including:
 - More detailed information about key fund activities, such as securities lending, derivatives investments, repurchase agreements and reverse repurchase agreements, including information about the counterparties and collateral for such activities;
 - Risk metric calculations to measure a fund’s exposure and sensitivity to changes in market conditions, such as changes in asset prices, interest rates and credit spreads;
 - The fund’s monthly returns.

The SEC is using a tiered approach to Form N-PORT compliance timeframes based upon fund complex assets under management. Fund complexes with net assets of \$1 billion or more will be required to file reports on Form N-PORT after June 1, 2018, but the SEC will make all N-PORT reports filed during the first six months following this date nonpublic. Fund complexes with less than \$1 billion in net assets will file reports on Form N-PORT one year later—after June 1, 2019. The rescission date for Form N-Q will be August 1, 2019.

The following table provides a comparison of the new reporting requirements under Form N-PORT and the previous reporting

requirements under Form N-Q (please note the table only includes those items deemed to be new or material requirements):

Reporting Information	Previous Reporting Obligations Under Form N-Q	New Reporting Obligations Under Form N-PORT	Comments
Reporting Schedule	Quarterly	Monthly	Every third report (quarterly) of Form N-PORT is made public.
Information About the Fund			
Assets invested in controlled foreign corporations	Yes	Yes	Form N-PORT requires a fund to disclose the amount of assets it has invested in a controlled foreign corporation (CFC) for the purpose of investing in certain types of instruments, including commodities.
Portfolio level risk	No	Yes	Form N-PORT includes portfolio risk metric calculations for funds with debt holdings that exceed 25% of the fund's net asset value (NAV) for the previous three months. The calculations disclose the change in a fund's portfolio value if interest rates change by one basis point and 100 basis points, respectively, for three-month, one-year, five-year, 10-year and 30-year maturities. A fund also must report its credit spread risk to show the change in its net asset value if credit spreads were to fluctuate by one basis point along the same maturities.
Securities lending information	No	Yes	<p>Form N-PORT requires a fund to provide the name and legal entity identifier (LEI) of each borrower, and the aggregate value of the securities on loan to the borrower. A fund must also report securities on loan in the schedule of investments. For each investment it must report (i) whether the investment is on loan, and if so, the value of the investment on loan; and (ii) whether any amount of the investment was a reinvestment of cash collateral or non-cash collateral, respectively, and if so, the dollar amount of the reinvestment.</p> <p>Additionally, a fund must disclose non-cash collateral not included in the schedule of investments, along with the aggregate principal amount, aggregate value and category of investments that most closely represent the collateral.</p>

Reporting Information	Previous Reporting Obligations Under Form N-Q	New Reporting Obligations Under Form N-PORT	Comments
Information About the Fund			
<p>Total returns</p> <p>Net realized gain (loss)</p> <p>Net change in unrealized appreciation (depreciation)</p>	No	Yes; for the preceding three months.	<p>A fund must now report standardized monthly total returns of the fund for the each of the preceding three months. The SEC views this information as useful for analysis and comparison among similar funds. Additionally, the Form N-PORT requires a fund to include the monthly net realized gains or losses and net change in unrealized appreciation or depreciation attributable to: (i) investments other than derivatives; and (ii) derivatives for each of the following asset categories: commodity contracts, credit contracts, equity contracts, foreign exchange contracts, interest rate contracts, and any other contracts. Within each asset category the fund will provide the same information for the following types of derivatives contracts: forward, future, option, swaption, swap, warrant, and other contracts.</p>
Schedule of Investments			
Repurchase agreements	Yes	Yes; with additional details.	<p>Additional information to be reported on Form N-PORT include with respect to repurchase and reverse repurchase agreements: (i) the name of the counterparty (and LEI if the agreement is not centrally cleared); (ii) repurchase rate; (iii) whether the agreement is a tri-party agreement; (iv) the maturity date; (v) the collateral principal amount, value and category of investments that best represents the collateral.</p>

Reporting Information	Previous Reporting Obligations Under Form N-Q	New Reporting Obligations Under Form N-PORT	Comments
Schedule of Investments			
Derivative contracts	No; Funds typically would provide this information in notes to the financial statements.	Yes; with additional details.	<p>Form N-PORT includes standardized formats to report derivative positions, including: (i) the type of derivative contract; and (ii) the name and LEI of the counterparty. Most notably, depending on the type of derivative contract, the fund may be required to provide detailed information on the underlying index or basket of investments and its components.</p> <p>A fund should include the index identifier for a derivative’s publically available underlying index. Non-public underlying indexes should be identified based on notional exposure:</p> <ul style="list-style-type: none"> • If the notional value of the contract is less than 1 percent of the fund’s net asset value (NAV), the index or basket should be identified with a narrative description. • If the notional value represents more 5 percent of the fund’s NAV, the fund should separately list and identify the index components with: (i) name; (ii) identifier; (iii) their number of shares or notional amount or contract value at trade date; and (iv) value at the close of the period. • If the notional value represents more than 1 percent but less than 5 percent of the fund’s NAV, the fund should provide the component information above but limit its reporting to (i) the 50 largest components of the index; and (ii) any other components that represent more than 1 percent of the notional value of the index.

Form N-CEN

New Form N-CEN replaces Form N-SAR as the SEC’s method to collect census information from investment companies. The adoption of Form N-CEN underscores the SEC’s shift to data-centric reporting that can be used to monitor and assess trends at the fund level and the market generally. In addition to disclosure that generally applies to all management investment companies, the Form gathers specific information dependent on the type of registrant. Form N-CEN will be filed in Extensible Markup Language format and includes many of the items now included in Form N-SAR, but also replaces items believed to be outdated and of limited usefulness. The Form will be filed with the SEC by all registered investment companies on an annual basis and no later than 75 days after the investment company’s fiscal year-end (for management companies) and calendar year-end (for UITs).

The SEC, unlike with Form N-PORT, will not use a tiered approach for compliance with Form N-CEN—all investment companies must file Form N-CEN after June 1, 2018, which will also be the rescission date for Form N-SAR.

The table below provides a comparison of key reporting requirements under Form N-CEN with the previous reporting requirements under Form N-SAR (please note, the table only includes those items deemed to be new or material requirements):

Form N-CEN in a Nutshell

- Filed annually by all funds 75 days after fiscal year-end or calendar year-end (UITs only)
- Replaces Form N-SAR
- Fund type-specific information, such as for ETFs or closed-end funds
- New disclosure requirements, including:
 - Fund director and chief compliance officer information;
 - Provisions of financial support and NAV corrections;
 - More detailed securities lending information, including counterparties, indemnifications received and fee/profit split among service providers.
- New ETF information, including:
 - Authorized participants, their trading volume and collateral posting requirements;
 - Creation and redemption statistics, including average fees.
- Closed-end funds and SBICs report secondary and rights offering information

Reporting Information	Previous Reporting Obligations Under Form N-SAR	New Reporting Obligations Under Form N-CEN	Comments
Registrant Information			
Reporting Schedule	Semi-Annually	Annually	
Director Information	No	Yes	Form N-CEN requires a fund to include (i) its directors’ full names; (ii) FINRA CRD numbers, if any; (iii) whether the directors are “interested persons” as defined under the Investment Company Act of 1940 (the “1940 Act”); and (iv) the 1940 Act file number of any other fund for which the director serves as a director.

Reporting Information	Previous Reporting Obligations Under Form N-SAR	New Reporting Obligations Under Form N-CEN	Comments
Registrant Information			
Chief Compliance Officer Information	No	Yes	Form N-CEN also requires a fund to include (i) its chief compliance officer's (CCO) full name; (ii) FINRA CRD number, if any; (iii) address and telephone number (the CCO's telephone number will not be made publically available on EDGAR); (iv) whether the CCO has changed since the registrant's last filing; and (v) whether the CCO is compensated or employed by any person other than the registrant or an affiliate of the registrant, and if so, the person's name and IRS Employer Identification Number.
Provision of Financial Support	No	Yes	A registrant must disclose in Form N-CEN whether it received financial support from an affiliate. The Form clarifies that fee waivers and expense reimbursements are exempted from this disclosure. If a fund receives support, it must provide a description of the support, including the affiliates involved and a description of the reason for the financial support.
Principal Underwriter's Information	Yes	Yes; with additional details.	Form N-CEN requests FINRA CRD numbers, Public Company Accounting Oversight Board (PCAOB) numbers and LEIs, and their state and country. The Form also asks whether the principal underwriter is affiliated with the registrant, its adviser or depositor and whether a principal underwriter was hired or terminated during the period.

Reporting Information	Previous Reporting Obligations Under Form N-SAR	New Reporting Obligations Under Form N-CEN	Comments
Registrant Information			
Independent Public Accountant Information	Yes	Yes; with additional details.	<p>Form N-CEN requests FINRA CRD numbers, PCAOB numbers and LEIs and whether the independent public accountant changed since the last filing.</p> <p>A fund must also indicate (i) whether the report on internal control noted material weaknesses; and (ii) whether the audit opinion issued was an unqualified opinion.</p> <p>A fund must file a copy of the independent public accountant's report on internal controls as an attachment to its reports.</p>
NAV Corrections	No	Yes; for open-end funds only.	A fund must indicate whether it made any payments or reprocessed shareholder accounts due to a net asset value (NAV) error. If yes, the fund should indicate the series by name and series ID number.
Rule 19a-1 Notice For Distributions	No	Yes; for management investment companies only.	A fund must indicate if, during the reporting period, it paid a dividend or distribution that required an accompanying Rule 19a-1 statement. If yes, the fund should indicate the series by name and series ID number.

Reporting Information	Previous Reporting Obligations Under Form N-SAR	New Reporting Obligations Under Form N-CEN	Comments
Management Investment Company Disclosure			
Type of Fund	Yes; whether the series is an index fund.	Yes; with additional details.	<p>Form N-CEN requires a fund to indicate its type from the following list: ETF or exchange-traded managed fund (ETMF); index fund; fund seeking to achieve performance results that are a multiple of an index or other benchmark, the inverse of an index or other benchmark, or a multiple of the inverse of an index or other benchmark; interval fund; fund of funds; master-feeder fund; money market fund; target date fund; and underlying fund to a variable annuity or variable life insurance contract.</p> <p>For certain fund types, the Form requires additional information. Index funds, for example, must indicate (i) whether the index is constructed by an affiliate; (ii) whether the index is exclusive to the fund; and (iii) the annualized difference between the fund's total returns and those of the index before and after fund fees and expenses. Master-feeder funds must provide identifying information for other funds in their master-feeder structure.</p>
Controlled Foreign Corporations	No	Yes	<p>Form N-CEN requires a fund to disclose whether it invests in a CFC for the purpose of investing in certain types of instruments, including commodities. The fund must also provide identifying information for the CFC. In seeking this information the SEC is attempting to determine whether there are any legal, tax or country-specific risks associated with the fund and the CFC.</p>

Reporting Information	Previous Reporting Obligations Under Form N-SAR	New Reporting Obligations Under Form N-CEN	Comments
Management Investment Company Disclosure			
Expense Limitations	No	Yes; with additional details.	<p>Form N-CEN requires the fund to indicate whether it engages in securities lending, provide the monthly average value of securities on loan and the net income from such activities. The fund must also indicate whether, during the period (i) a borrower failed to return a security resulting in liquidation of pledged collateral and/or an adverse impact to the fund; (ii) the fund is indemnified against borrower default by the securities lending agent or any other entity; and (iii) the fund exercised its indemnification rights.</p> <p>Additionally, the Form requires the fund to provide identifying information for the securities lending agent and any securities lending cash collateral manager.</p> <p>Form N-CEN also requires a fund to identify the types of fees it pays in relation to the securities lending arrangement, and describe the share of revenues and fees amongst the fund, the securities lending agent and any cash collateral manager.</p>
Service Provider Information	Yes	Yes; with additional details.	<p>Form N-CEN has added the transfer agent and pricing services to the service providers that are currently included in Form N-SAR—the fund’s adviser(s) or sub-adviser(s), administrator, principal underwriter, sub-transfer agents, shareholder servicing agent, independent public accountant, affiliated broker/dealer, custodian/sub-custodian.</p> <p>Form N-CEN, unlike Form N-SAR, requires the fund to indicate whether the service provider is affiliated with the fund or its adviser, and whether any service provider was hired or terminated during the period.</p> <p>Form N-CEN requires a fund to identify its shareholder servicing agents and sub-shareholder servicing agents. Provision of this information is in line with the SEC’s focus on whether fees for distribution are paid out of fund assets and outside of the fund’s 12b-1 plan.</p>

Reporting Information	Previous Reporting Obligations Under Form N-SAR	New Reporting Obligations Under Form N-CEN	Comments
Closed-End Management Company and Small Business Investment Company Disclosure			
Secondary and Rights Offerings	No	Yes	The Form requires closed-end funds and SBICs to report whether they made any secondary or rights offerings and if so, the type of security offered (e.g. common stock, bonds). The Form also requests the percentage of rights that were exercised.
ETF and ETMF Disclosure			
Authorized Participants	No	Yes	ETFs and ETMFs will be required to provide identifying information for each authorized participant (AP) of the fund. The fund must also provide the dollar value of fund shares the AP purchased and redeemed, respectively, during the period. Form N-CEN also requires ETFs and ETMFs to indicate whether the AP was required to post collateral in connection with its purchase or redemption activity.
Creation Units	No	Yes	<p>Form N-CEN requires ETFs and ETMFs to report the number of shares required to form a creation unit. The funds must also disclose, based on the dollar value paid for each creation unit both purchased and redeemed, respectively, by APs during the reporting period: (i) the average percentage of that value composed of cash; (ii) the standard deviation of the percentage of that value composed of cash; (iii) the average percentage of that value composed of non-cash assets and other positions exchanged on an in-kind basis; and (iv) the standard deviation of the percentage of that value composed of non-cash assets and other positions exchanged on an in-kind basis.</p> <p>ETFs and ETMFs must also disclose the average transaction fees charged to APs for creation unit transactions that transact fully or partially on a cash-basis and those that transact fully in-kind, respectively.</p>

Reporting Information	Previous Reporting Obligations Under Form N-SAR	New Reporting Obligations Under Form N-CEN	Comments
ETF and ETMF Disclosure			
Benchmark Return Difference (UITs only)	No	Yes	The Form requires index ETFs to indicate whether their index is exclusively constructed for the fund and/or managed by an affiliate. The ETF must also include its tracking error and tracking difference during the period—gross and net fees and expenses.

Regulation S-X and Form N-1A Amendments

The Modernization Rules amend Regulation S-X in an effort to increase transparency related to derivatives and their counterparties. Importantly, the amendments bring derivatives into the schedule of investments and add standardized schedules for futures contracts, forward foreign currency contracts and swap contracts. The SEC anticipates that the amendments cover most, if not all, types of derivatives contracts held by investment companies. Additionally, the Regulation S-X amendments enhance reporting of options contracts. The amendments to Regulation S-X will take effect on August 1, 2017.

The table below provides a brief summary of the new rules added to Regulation S-X.

Rule	Description
12-13 - (Open option contracts written)	The amendments renumber previous Rule 12-12B to Rule 12-13 and also change reporting of open options contracts. Previously, a fund was required to report: (i) the name of the option's issuer; (ii) the number of contracts; (iii) exercise price; (iv) expiration date; and (v) the option's value. The new rule, Rule 12-13, requires a fund to report the: (i) description of the option, including an underlying index or basket of securities; (ii) the counterparty (except exchange-traded and centrally cleared options); (iii) number of contracts; (iv) notional amount; (v) exercise price; (vi) expiration date; and (vii) the option's value.
12-13A - (Open futures contracts)	Many funds currently report open futures contracts in the notes to financial statements, but new Rule 12-13A standardizes the disclosure of open futures contracts. The rule requires a fund to report the (i) description of the contract; (ii) number of contracts; (iii) expiration date; (iv) notional amount; (v) value; and (vi) unrealized appreciation or depreciation.
12-13B - (Open forward foreign currency contracts)	Much like futures contracts, a large number of funds currently report open forward foreign currency contracts in the notes to financial statements. New Rule 12-13B standardizes reporting of forward foreign currency contracts. The new rule requires a fund to report the: (i) amount and description of the currency to purchased; (ii) amount and description of the currency to sold; (iii) counterparty; (iv) settlement date; and (v) unrealized appreciation or depreciation.

Rule	Description
12-13C - (Open swap contracts)	Rule 12-13C standardizes how funds report their swap positions. Under previous Rule 12-13, a fund reported the: (i) description of the swap (including the maturity date and the payments to be paid and received); (ii) the notional amount; and (iii) unrealized appreciation or depreciation. New Rule 12-13C incorporates those reporting requirements and also requires a fund to report the: (iv) swap counterparty's information (except exchange-traded and centrally cleared options); (v) the swap contract's value; and (vi) related upfront payments or receipts. Consistent with new Rule 12-13 for options contracts, swaps contracts with an underlying index or basket of securities must describe the underlying index or basket of securities.

Additional Regulation S-X Amendments

The Modernization Rules made several additional administrative and technical amendments to Regulation S-X to renumber rules and modify current reporting requirements to conform to the new reporting rules. Among the additional amendments:

- **Rule 12-12—Investments in securities of unaffiliated issuers:** A fund must indicate securities that are on loan. Also, variable rate debt should be reported with the referenced rate and spread, along with the end of period interest rate and maturity. Payment-in-kind securities should be disclosed with the rate paid in-kind.
- **Amendments under Rule 12-14—Investments in and advances to affiliates:** under Rule 12-14, a fund should (i) report the net realized gain or loss for the period and net increase or decrease in unrealized appreciation or depreciation for the period for each investment disclosed under Rule 12-14; and (ii) make the categorization of investments consistent with those methods used in Rules 12-12, 12-12A and 12-12B.

The amendments to Regulation S-X will take effect on August 1, 2017.

Form N-1A Amendments

The Modernization Rules have amended Forms N-1A and N-3, and Form N-CSR (for closed-end funds only) to require funds to disclose securities lending income and fees and compensation paid to securities lending agents in their statements of additional information. A fund must also describe the services provided by the securities lending agent. The amendments to Forms N-1A, N-3 and N-CSR will take effect on August 1, 2017.

Suggested Actions for Investment Companies

- **Review Fund Operations and Technical Capabilities:** Service providers should review their technological capabilities and assess changes needed to ensure they will be able to collect, process and present the needed information for the reports. It will be important to identify early the sources of data that will be needed to comply with the reporting obligations.
- **Director Oversight:** Fund directors should be apprised of the new rules and how they will impact the funds and their reporting obligations. Directors may consider requesting regular status updates from the service providers as they prepare to meet the new reporting obligations.

For more information on the application of the rules or investment company regulatory compliance, please contact one of the authors listed below or the Drinker Biddle Investment Management Group lawyer with whom you regularly work.

[1] The adopting release for the Modernization Rules can be found on the SEC [website](#).

Investment Management Group

Primary Contacts



Diana E. McCarthy
Partner
Philadelphia
(215) 988-1146
Diana.McCarthy@dbr.com



Benjamin D. McCulloch
Associate
Chicago
(312) 569-1109
Benjamin.McCulloch@dbr.com

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