

New Fund Shareholder Report & Advertising Rules

In a rare unanimous vote, the SEC approved on October 20, 2022 a [final rule](#) with comprehensive changes to the mutual fund and exchange-traded fund (ETF) disclosure framework. The rule also updates advertising rules for registered investment companies (RICs) and business development companies (BDCs) to include certain standardized figures and reasonably current information.



Background

Fund shareholders typically receive an updated prospectus annually, as well as annual and semiannual shareholder reports. These shareholder reports provide detailed information about a fund's operations and activities during the last full- or half-year period. A SEC staff analysis indicates many shareholders disregard existing fund reporting as being overly long and complex and, as a result, spend little or no time reviewing the documentation that is costly to print and mail; costs ultimately borne by shareholders.

Under the final rule, the types of fund information would remain largely unchanged; however, the detailed information more relevant to financial professionals and analysts would be available online and delivered upon request to fund shareholders who want that additional information.

A. Tailored Shareholder Reports

Mutual funds and ETFs registered on Form N-1A will be required to transmit concise and visually engaging annual and semiannual reports (three to four pages in length) that highlight key information (fund expenses, performance, and portfolio holdings) focused on retail shareholders to assess and monitor fund investments. Certain information that may be more relevant to financial professionals and investors who desire more in-depth information will no longer appear in funds' shareholder reports but will be available online, delivered free of charge upon request, and filed on a semiannual basis on Form N-CSR.

An outline of the new shareholder report format is included in [Appendix A](#). Changes to the annual report contents are detailed in [Appendix B](#).

The amendments do not apply to other investment companies such as closed-end funds, unit investment trusts (UITs), or open-end managed investment companies not registered on Form N-1A, i.e., issuers of variable annuity contracts registered on Form N-3.

Shareholder Reports

New Item 27A to Form N-1A specifies the design and content of funds' annual and semiannual reports. The final rules will generally allow a fund to include in its annual report only the information that Item 27A of Form N-1A specifically permits or requires. If a fund's circumstances may cause the required disclosures to be misleading, the final rules will allow a fund to add information to the report that is necessary to make the required disclosure items not misleading, which should be brief. If a required disclosure is inapplicable, a fund may omit the disclosure. A fund also may modify a required legend or narrative information if the modified language contains comparable information to what is otherwise required. A fund is not permitted to incorporate by reference any information into its annual report. Funds will be required to refer shareholders to the availability of certain additional website information near the end of the report. Funds are allowed to provide additional information to shareholders in the same transmission as the shareholder report, if the shareholder report is given greater prominence than any other materials, except for certain specified disclosure materials (summary prospectuses, statutory prospectuses, notices of the online availability of proxy materials, and other shareholder reports).

Under the final rule, a fund must prepare separate annual reports for **each series of a fund** so that a fund shareholder will receive an annual report that addresses only the series in which that shareholder is invested. Currently, a fund registrant might prepare a single shareholder report that covers multiple series.

While certain shareholder report disclosures will be the same for all classes, details on some share classes could vary significantly, *i.e.*, expense charges or performance date fund returns. Therefore, a fund must prepare and transmit to the shareholder a shareholder report that covers the **single class of a multiple-class fund** in which the shareholder invested. The SEC acknowledged that shareholders could benefit from information about the other share classes offered by a multiple-class fund and added a requirement to post to the web fund documents that will enable investors to obtain information about those other share classes easily.

Management's Discussion of Fund Performance (MDFP)

These disclosures would be more concise while largely maintaining current requirements. The disclosure must "briefly summarize" the "key" factors that materially affected the fund's performance during the last fiscal year, including the relevant market conditions and the investment strategies and techniques used by the fund's investment adviser. Funds should not include lengthy, generic, or overly broad discussions of these factors. Funds are not allowed to include any additional information—such as a fund president's letter to shareholders, interviews with portfolio managers, general market commentary, and other similar information—in the shareholder report.

The final rule updates requirements for the performance line graph. The graph must show the performance of a \$10,000 investment in the fund and in an appropriate broad-based securities market index¹ over a 10-year period. A fund has the option to compare its performance to other indexes, including more narrowly based indexes that reflect the market sectors in which the fund invests. Funds no longer have the option to show periods longer than 10 years.

The final rule adds two items to the performance table—the average annual total returns of an appropriate broad-based securities market index and the fund's average annual total returns without sales charges (in addition to the current disclosure showing returns reflecting applicable sales charges). Funds could add a brief disclosure to contextualize the line graph and average annual returns table. Specifically, if a material change occurred to the fund during the relevant performance period, such as a change in investment adviser or a change to the fund's investment strategies, the fund may include a brief legend or footnote to describe the change and when it occurred.

¹ Defined in the final rule as an index that represents the overall applicable domestic or international equity or debt markets

Under the final rules, a fund with a stable distribution policy would need to disclose if it was unable to maintain the specified level during the past fiscal year.

Consistent with current rules, money market funds are not required to include MDFP.

Fund Statistics

Fund statistics that must be included in the annual report:

- Net assets
- Total number of portfolio holdings
- For funds other than money market funds, portfolio turnover rate
- The total advisory fees paid by the fund during the reporting period

A fund is permitted to disclose any additional statistics that the fund believes would help shareholders better understand the fund's activities and operations during the reporting period. Fund statistics must precede any additional permitted statistics the fund chooses to include. If a statistic is included in—or could be derived from—a fund's financial statements or financial highlights, the most recent financial statements or financial highlights must be used. A fund could briefly describe the significance or limitations of any disclosed statistics in a parenthetical or similar presentation.

Graphical Representation of Holdings

Most existing requirements have been retained. Funds are now permitted to show their holdings based on total exposure to particular categories of investments in addition to ones currently available. This can be in tabular or graphical format. A fund may include—along with the graphical representation of holdings—a list of its largest 10 portfolio holdings and the percentage of the fund's net asset value, total investments, or total exposure attributable to each such holding.

B. Form N-CSR Changes & Online Requirements

Certain information currently included in a fund's annual and semiannual reports may be less relevant to retail shareholders and of more interest to financial professionals and those investors who desire more in-depth information. Under the final rule, this information would be available online, delivered free of charge upon request, and filed with the SEC on a semiannual basis on Form N-CSR.

Form N-CSR Additions

- **Financial Statements.** Currently, Section 30(e) of the Investment Company Act provides that funds' annual and semiannual reports include the fund's financial statements, consisting of a statement of assets and liabilities, a schedule of investments that shows the amount and value of each security owned by the fund on that date, a statement of operations, and a statement of changes in net assets. The annual report must include audited financial statements accompanied by a certificate of an independent public accountant. Regulation S-X establishes general requirements for portfolio holdings disclosures in fund financial statements. Under the final rule, complete audited annual and unaudited semiannual financial statements would be filed with Form N-CSR rather than the shareholder report. Form N-1 has been amended to eliminate a fund's ability to provide a summary schedule in lieu of providing a complete schedule of portfolio investments as part of the financial statements. Form N-CSR amendments do not prohibit funds from preparing and submitting multicolumn financial statements that include multiple series or portfolios,

or that address multiple share classes of a fund, provided such financial statement presentation is consistent with Regulation S-X.

Only certain data points from the financial statements would be included in the annual and semiannual reports, including a summary schedule of portfolio positions. Consistent with current requirements, the fund's annual financial statements must be audited by an independent public accountant and accompanied by any associated accountant's report, while the semiannual financial statements need not be audited.

- **Financial Highlights.** This information is identical to the information currently required in fund shareholder reports and includes a summary table² of financial information covering the preceding five years (or since the fund's inception, if less than five years). The expense ratio and net assets and portfolio turnover rate will continue to be included in annual or semiannual reports.
- **Changes in and Disagreements with Accountants.** Under the final rule, a fund must file on Form N-CSR the disclosures that Item 304 of Regulation S-K currently requires, concerning changes in and disagreements with accountants that are now included in shareholder reports. Going forward, funds would include a high-level summary of changes in and disagreements with accountants in their annual reports.
- **Matters Submitted for a Shareholder Vote.** Shareholders will continue to receive a detailed description of matters submitted for a shareholder vote in fund proxy statements, as they do today. This information will now be included on Form N-CSR, unless the information is already disclosed as part of the financial statements.
- **Remuneration Paid to Directors, Officers, and Others.** Under §30(e) of the Investment Company Act, funds currently provide the aggregate remuneration the fund paid to its directors, officers, and certain affiliated persons in shareholder reports.
- **Statement Regarding Basis for Approval of Investment Advisory Contract.** Funds currently are required to provide a statement—in the annual and semiannual reports—regarding the basis for the board's approval of the fund's investment advisory contract. The final rules will instead require funds to provide this information on Form N-CSR.

A fund's principal executive and financial officer are required to certify the financial and other information included on Form N-CSR, and they are subject to liability for material misstatements or omissions on Form N-CSR.

Website Requirements

The information that is **newly required in Form N-CSR** and no longer included in shareholder reports must be available on a website, publicly accessible, and free of charge. This information must be available from 60 days³ after the end of the relevant fiscal period until 60 days following the end of the next respective fiscal period. The 60-day time frame for availability is consistent with the current requirement to transmit shareholder reports to investors.

² The summary table contains information about changes in a fund's net asset value, total returns, portfolio turnover rate, and capital distributions, among other things, during the preceding five years.

³ The final rule includes a safe harbor. A fund would satisfy its transmission obligations even if it did not meet the rule's posting requirements for a temporary period of time. To rely on this safe harbor, a fund must have reasonable procedures in place to help ensure that the required materials appear online and also must take prompt action to correct noncompliance with the rule's website availability requirements. Prompt action is required as soon as practicable following the earlier of the time at which the fund knows—or reasonably should have known—that the required documents are not available.

Funds will continue to have 70 days to file the complete Form N-CSR with the SEC.

A fund's complete portfolio holdings will be available online in a fund's financial statements for the second and fourth quarters. The final rule adds a requirement for a fund (other than a money market fund) to make its complete portfolio holdings for the first and third fiscal quarters available on a website within 60 days after the close of each quarter, which must remain publicly accessible online for a full fiscal year. This change provides investors with a full year of complete portfolio holdings in one location.

The website address with the required information must be specified on the cover page or beginning of the shareholder report and cannot be the address of the SEC's electronic filing system. The website may not be the home page or section of the fund's website other than on which the information is posted. An investor must be able to navigate from the landing page to each of the required documents with a single click or tap. Online materials must be presented in a format convenient for both reading online and printing on paper, and persons accessing the materials must be able to retain permanently (free of charge) an electronic copy of the materials in this format. A fund must send—at no cost—either a paper copy or electronic copy as requested of any of the online materials within three business days of the request.

Funds will have the option to post the most recently completed Form N-CSR to its website to satisfy the new website availability requirements.

Items Removed from Shareholder Reports & Form N-CSR

The final rule eliminates the following items currently in the shareholder report with no obligation to include on Form N-CSR:

- Management information table. Identical information will remain available in a fund's statement of additional information⁴ (SAI), which is available online or delivered upon request.
- Liquidity risk management program. Information relevant to funds' liquidity risk and risk management will remain available on Form N-PORT, on Form N-CEN, and in funds' prospectuses.

C. Exclusion of Open-End Funds from Rule 30e-3

Rule 30e-3, first effective in January 2021, generally permits funds to satisfy shareholder report transmission requirements by making these reports and other materials available online and providing a notice of the reports' online availability with a hyperlink, instead of directly providing the reports to shareholders. Because the SEC expects open-end shareholders to benefit from the above changes, the final rule excludes open-end funds from Rule 30e-3. Shareholders in open-end funds will directly receive the new tailored annual and semiannual reports, in paper form, or if elected, electronically.

The final rule does not affect the availability of Rule 30e-3 for other registered management companies (such as registered closed-end funds) or registered UITs.

⁴ Funds are not required to provide investors with the SAI, but they must provide it for free upon request. This also is known as Part B of the fund's registration statement.

D. Investment Company Advertisements

These changes will apply to all investment companies that are subject to the SEC's advertising rules, including mutual funds, ETFs, registered closed-end funds, and BDCs. The rule requires that presentations of investment company fees and expenses in advertisements and sales literature are consistent with relevant prospectus fee tables and reasonably current, and also addresses materially misleading fund fee and expense presentation. Current advertising rules focus primarily on performance-related information with very little focus on fees and expenses. As funds are increasingly marketed on the basis of costs, the SEC was concerned that investment companies may understate or obscure the costs of a fund investment.

Required Fee & Expense Figures (Rule 482)

Rule 482 establishes the content, legend, and filing requirements for investment company advertisements. Rule 482 is amended so that investment company advertisements providing fee and expense figures must now include both:

- The maximum amount of any sales load, or any other nonrecurring fee
- The total annual expenses without any fee waiver or expense reimbursement arrangement (collectively, the "required fee and expense figures") based on the methods of computation for a prospectus that the fund's registration statement form prescribes for those figures

An advertisement would not need to include the required fee and expense figures if it only included general, narrative information about fee and expense considerations and did not include any numerical fee or expense amounts.

The final rule makes conforming amendments to Rules 34b-1 and 433 to incorporate Rule 482's requirements for required fee and expense figures. This ensures that the same fee and expense-related requirements are applied consistently across RIC and BDC advertisements and sales literature. Regardless of whether an advertisement is in the form of a Rule 482 advertisement or Rule 34b-1 supplemental sales literature, or whether a registered closed-end fund or BDC advertisement uses Rule 482 or Rule 433 for a free writing prospectus, the advertisement would be subject to the same requirements regarding fee and expense information.

Prominence, Fee Waivers & Expense Reimbursements, & Timeliness

The final rule permits investment company advertisements to include other figures about a fund's fees and expenses in addition to the required fee and expense figures noted above. Those advertisements will have to present the required fee and expense figures at least as prominently as any other included fee and expense figures. For example, an advertisement could include a fund's fees and expenses net of certain amounts, such as a fee waiver or expense reimbursement arrangement, but could not present the net figure more prominently than the required fee and expense figures.

Advertisements that include a fund's total annual expenses net of fee waiver or expense reimbursement arrangement amounts also must include the arrangement's expected termination date.

Fee and expense information will need to be as of the date of the fund's most recent prospectus or—if the fund no longer has an effective registration statement—as of its most recent annual report. A fund will, however, be able to provide more current information, if available.

Materially Misleading Statements (Rule 156)

Rule 156 applies to sales literature used by any person to offer to sell or induce the sale of securities of any investment company, including RICs and BDCs. Currently, Rule 156 broadly prohibits the use of materially misleading sales literature in connection with the offer or sale of securities issued by an investment company. The amendments to Rule 156 specifically address practices that could lead to materially misleading representations about fees and charges. Representations about an investment fund's fees or expenses could be misleading because of statements or omissions involving a material fact, including situations where portrayals of the fees and expenses associated with an investment in the fund omit explanations, qualifications, limitations, or other statements necessary or appropriate to make the portrayals not misleading. The final rule includes an example of funds that market themselves as "zero expense" or "no expense funds" without mentioning other costs, e.g., securities lending fees, investors would incur when investing in the fund.

Whether a particular description, representation, illustration, or other statement involving a fund's fees and expenses is materially misleading depends on evaluation of the context in which it is made.

These amendments apply to all investment company sales literature, regardless of whether the investment company's prospectus contains total annual expense figures.

Conclusion

The asset management team at **FORVIS** has more than 50 years of experience providing accounting, tax, and consulting services to various types of investment holdings, including conventional debt and equity investments, loans, businesses, alternative investments, and other unique assets. As of August 2022, Convergence Optimal Performance ranked FORVIS as a top 25 accounting and audit firm to registered investment advisors. FORVIS was also ranked in the top 20 by assets under management. We have experience providing services to fund complexes with net assets ranging from a couple million to several billion dollars. Our experience allows us to provide tailored services to help meet your unique needs.

For more information, visit forvis.com.

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Appendix A

The following table outlines the information funds must include in their annual reports:

Annual Report Outline	
	Description
Cover page or beginning of report	Fund/Class Name
	Ticker Symbol
	Principal U.S. Market(s) for ETFs
	Statement Identifying as “Annual Shareholder Report”
	<p>Legend – “This annual shareholder report contains important information about [the Fund] for the period of [beginning date] to [end date]. You can find additional information about the Fund at [Fund website address]. You can also request this information by contacting us at [toll-free telephone number and, as applicable, email address].”</p> <p>Statement on Material Fund Changes in the Report – “This report describes changes to the Fund that occurred during the reporting period.” This would include changes in a fund’s name, investment objective or goals, operating expenses, fees, principal investment strategies, principal risks, or investment advisers.</p>
Content	<p>Expense Example – A fund will be required to provide a table showing the expenses associated with a hypothetical \$10,000 investment in the fund during the preceding reporting period in two formats: (1) as a percent of a shareholder’s investment in the fund, <i>i.e.</i>, expense ratio, and (2) as a dollar amount.</p>
	<u>Management’s Discussion of Fund Performance</u>
	<u>Fund Statistics</u>
	<u>Graphical Representation of Holdings</u>
	Material Fund Changes
	<p>Changes in and Disagreements with Accountants – When a fund has a material disagreement with an accountant that has resigned or been dismissed, a fund must include in its annual report</p>

whether the former accountant resigned, declined to stand for re-election, or was dismissed and the date as well as a brief, plain English description of disagreement(s) with the former accountant during the fund's two most recent fiscal years and any subsequent interim period that the fund discloses on Form N-CSR.

Availability of Additional Information – A brief, plain English statement in the shareholder report that informs investors about certain additional information that is available on the fund's website.

Householding Disclosure (optional) – Funds relying on the householding provision (single report to multiple members of a household) must explain to investors who have provided written or implied consent how they can revoke their consent.

Appendix B

The table below summarizes the contents that funds will include in their annual reports—or, alternatively, that they will file on Form N-CSR—in comparison to current shareholder report disclosure requirements.

Changes to the Annual Report Contents	
Current	Final Rule – Description of Amendments
	NEW – Identifying information – see cover page details in Appendix A
Expense example	Retain in annual report in a more concise form
<u>MDFP</u>	Retain in annual report in a more concise form
	Add new <u>fund statistics</u> section to the annual report
Graphical representation of holdings	Retain in annual report
	Add new material fund changes section to the annual report
Changes/disagreements with accountants	Retain in annual report in summary form. The entirety of the currently required disclosure would move to Form N-CSR
Availability of quarterly portfolio schedule, proxy voting policies and procedures, and proxy voting record	Include a more general reference to the availability of additional fund information in the annual report
	Add householding provision (optional)

Moved to Form N-CSR	
(Must be available online and delivered (in paper or electronic form) upon request)	
Financial statements, including schedule of investments	Move to Form N-CSR
Financial highlights	Retain certain data points, but generally move to Form N-CSR
Results of shareholder proxy votes	Move to Form N-CSR
Remuneration paid to directors, officers, and others	Move to Form N-CSR
Basis of board's approval of investment advisory contract	Move to Form N-CSR
Removed from Shareholder Reports	
Availability of additional information about fund directors	Remove from shareholder reports. Information would remain available in a fund's SAI either online or delivered upon request
Liquidity Risk Management Program	Remove from shareholder reports
Rule 30e-3 disclosures	Remove from shareholder reports
President's letter	Disclosures are restricted to items permitted by Item 27A of Form N-1A (other materials may accompany the transmission of the report if they meet the prominence requirement for material that accompanies the report)