



# MUTUAL FUND DIRECTORS FORUM

*The FORUM for FUND INDEPENDENT DIRECTORS*

August 16, 2022

Ms. Vanessa Countryman  
Secretary  
United States Securities and Exchange Commission  
100 F Street NE  
Washington, DC 20549

Re: Investment Company Names (File No. S7-16-22)

Dear Ms. Countryman:

The Mutual Fund Directors Forum (“the Forum”)<sup>1</sup> welcomes the opportunity to comment on the Commission’s recent rule proposal designed to provide investors with greater clarity regarding a fund’s particular investments and risks based on certain terms used in fund names.<sup>2</sup> We broadly agree that certain fund names provide investors with important indications about a fund’s investments. However, as we discuss in more detail below, we have concerns that the rule will constrain both innovation and investment decision-making for funds whose names would fall within the rule.

The Forum is an independent, non-profit organization for investment company independent directors and is dedicated to improving mutual fund governance by promoting the development of concerned and well-informed independent directors. Through education and other services, the Forum provides its members with opportunities to share ideas, experiences and information concerning critical issues facing investment company independent directors and also serves as an independent vehicle through which Forum members can express their views on matters of concern.

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We agree with the Commission that fund names play an important role in conveying to fund investors the investment thesis of a fund in which they are or are considering investing in, whether that thesis is that the fund invests in a specific type of security, a specific geography, a

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<sup>1</sup> The Forum’s current membership includes over 1000 independent directors, representing 145 mutual fund groups. Each member group selects a representative to serve on the Forum’s Steering Committee. This comment letter has been reviewed by the Steering Committee and approved by the Forum’s Board of Directors, although it does not necessarily represent the views of all members in every respect.

<sup>2</sup> See Investment Company Names, Release Nos. 33-11067, 34-94981, and IC-34593 (File Nos. S7-16-22), 87 Fed. Reg. 36594 (June 17, 2022) (*hereinafter* “Proposing Release”).

specific industry or employs a particular investment strategy. Given the importance of fund names, we welcome the Commission's reexamination of the rule.

Broadly, we agree that fund names can, in certain circumstances, be misleading, and that it is appropriate for the Commission to take action to prevent investors from being misled by inaccurate fund names. However, as the Commission has recognized in the past, a fund name must be considered in the context of other information available about the fund, including, most notably, the fund's own description of its investment process. The Commission's statement when it adopted the initial Names Rule, that "investors should not rely on an investment company's name as the sole source of information about a company's investments and risks," is as true today as it was twenty years ago.

### **1. Application of Names Rule to Strategy-Based Terms**

One of the primary benefits of the current names rule is the degree of certainty and comparability that it provides for the types of names currently covered by the rule. For example, with respect to a fund that has the term "Europe" in its name, an investor can be relatively assured that 80% or more of the fund's portfolio will consist of European securities irrespective of whether it is a European Growth Fund, European Value Fund or European Income Fund. An investor in such a fund can and should readily understand that the fund will primarily invest in securities that are European.

This is significantly less true when applied to a strategy rather than a category or classification of securities. For example, while investors generally understand what constitutes a "growth stock" or "growth stock strategy" (or, conversely, a "value stock" or "value stock strategy"), there is certainly no generally accepted way to classify any stock or strategy as one or the other. Thus, among the range of available growth stock funds, it is hardly surprising that there are numerous different definitions of what constitutes a growth stock and numerous different approaches to executing a growth stock strategy. Given this – as the Commission's admonition in 2001 that investors should not rely solely on a fund's name in making an investment decision – the presence of "growth" in the fund's name is of limited use to an investor considering a fund, unless that investor also reads and considers the description of the fund's strategy. Therefore, while requiring the fund to invest 80% of its portfolio in securities it considers consistent with its definition of "growth" is not useless, it provides significantly less investor protection than the application of the 80% requirement to terms like "European."

Our concern is particularly pronounced as applied to funds that use ESG terms such as "sustainable," "environmental" or "socially conscious" in their names. These terms are even less susceptible to a clear definition than terms like "growth" or "value," and hence, for any investor considering the fund, reading and understanding how the fund defines these terms and applies them in executing its investment strategy is critically important. No investor should place significant reliance on this type of name alone, and to the extent that the current proposal implies that an investor should be able to derive assurance from the fund name, it is misguided. The Commission should be wary of adopting an overly rigorous approach with respect to fund names that indicate that the fund pursues a specific investment strategy.



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## **2. Integration Fund Use of ESG Terminology**

Separately, we are troubled by the Commission's proposal that the use of an ESG term in its name by an ESG Integration Fund is materially deceptive. We understand the Commission's concern that there is a risk that an ESG term could be used by a fund in its name more for marketing purposes than as an accurate description of the fund's investment approach. However, as in other circumstances involving misleading fund names, the Commission has significant antifraud authority to address this issue. In contrast, as investor interest in ESG investing has grown, the marketplace has been very dynamic in developing different approaches to bringing an ESG lens to various investment strategies. The Commission's approach here risks largely limiting the use of ESG terms in fund names to funds that use inclusionary or exclusionary screens (as well to the limited number of funds that employ impact or proxy-voting strategies).

Given the range of ESG strategies that continue to evolve, we believe that the Commission's proposed approach does both a disservice to investors and risks hindering further innovation in the ESG space. We encourage the Commission to drop this requirement and instead use its antifraud authority to pursue any fund that clearly misleads investors through the use of an ESG term in its name.

## **3. Returning to Compliance**

We also encourage the Commission to adopt more flexibility with respect to a fund's need to return its portfolio to compliance with the names rule. While we agree that in most circumstances, a fund should be able to return to compliance within 30 days, it is difficult to anticipate every type of market volatility or other extenuating circumstance that might make this difficult to do while still protecting the interests of the fund's shareholders. Instead, as the Commission's request for comments on this part of the proposal suggests, boards can play an important role. We suggest that the Commission permit a fund to have additional time to return to compliance with the 80% requirement only if the board, based on notice from the fund's adviser, concludes that a longer timeframe is in the best interests of the fund's investors and agrees to a specific plan to bring the fund back into compliance. While we believe that circumstances necessitating this finding would rarely occur, allowing funds and boards this option would provide important protections for fund investors in rare and unexpected circumstances.

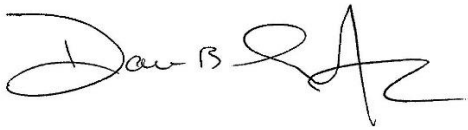
## **Conclusion**

As noted above, we appreciate the Commission's reexamination of the Names Rule but note the importance of conveying to investors that a fund's name should not be the sole measure of the fund's investment strategy and activities. Additionally, while we believe the Commission can play an important role in bringing clarity to the ESG investment space for investors, certain parts of the rule as currently proposed may prevent innovation in the fund space. Lastly, we would encourage the Commission to adopt more flexibility with respect to a fund's need to return its

portfolio to compliance and believe a fund's board of directors could play an important role in safeguarding investor interests.

We thank the Commission for its work on this proposal and welcome the opportunity to discuss these comments in further detail. Please feel free to contact David Smith, the Forum's General Counsel, at [david.smith@mfdf.org](mailto:david.smith@mfdf.org) or 202-507-4491 or Carolyn McPhillips, the Forum's President, at [carolyn.mcphillips@mfdf.org](mailto:carolyn.mcphillips@mfdf.org) or 202-507-4493.

Sincerely,

A handwritten signature in black ink, appearing to read "David B. Smith, Jr.", with a stylized flourish at the end.

David B. Smith, Jr.  
Executive Vice President & General Counsel