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THE SEC'S PROPOSED CHANGES TO ITS NAMES RULE

In this article, the authors discuss the SEC's proposed changes to its names rule (Rule 35d-1) in detail. They begin with the statutory and regulatory background. They then turn to the proposed rule changes, observing at the outset that the proposal would dramatically expand the universe of terms that would be covered by the rule. They then discuss other topics related to a fund's announced 80% investment policy. They conclude with a critique of the proposal's interpretive uncertainty and compliance burden.

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On May 25, 2022, the SEC proposed changes to Rule 35d-1 ("the Proposal") under the Investment Company Act of 1940.[1] Rule 35d-1 currently provides a framework for applying Section 35(d) of the 1940 Act's prohibition on the use of materially deceptive or misleading names. Rule 35d-1 requires funds whose names contain certain terms to invest, under normal circumstances, at least 80% of their assets in the type of investments suggested by such terms. The Proposal would significantly expand the scope of fund names that are subject to the rule, impose a new ongoing compliance requirement, narrow the circumstances under which a fund may depart from an 80% investment policy, and impose new disclosure and testing requirements.

This article examines the statutory and regulatory backdrop against which these changes are proposed, provides an overview of the Proposal, and identifies significant challenges the Proposal would pose if adopted in its current form.

[1] Inv. Co. Act Rel. No. IC-34593 (2022) ("Proposing Release").

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I. STATUTORY BACKGROUND

As initially enacted, Section 35(d) of the 1940 Act provides that "[i]t shall be unlawful for any registered investment company hereafter to adopt as a part of the name or title of such company, or of any security of which it is the issuer, any word or words which the Commission finds and by order declares to be deceptive or misleading."[2] Section 35(d) is, in essence, anti-fraud provision premised on truth-in-advertising principles. In its original form, Section 35(d) required that the SEC declare a particular fund name to be deceptive or misleading and then to pursue a claim against the fund in federal court to prohibit its further use.[3] However, given the statute's "extremely cumbersome" procedural hurdles, it was rarely invoked.[4] To address this, as part of the National Securities Markets Improvement Act of

[2] § 80a-34(d) (1940).

[3] *Id.*; Inv. Co. Act Rel. No IC-24828 (2001) (hereinafter, the "2001 Adopting Release").

[4] H.R. Rep No. 104-622, at 50 (1996).