SEC STAFF ISSUES STATEMENT ON THE REVIEW OF RULE 485(A) FILINGS

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U.S. Investment Management Alert

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On April 2, 2019, the Division of Investment Management (the "Division") at the Securities and Exchange Commission ("SEC") issued Accounting and Disclosure Information 2019-07 (the "ADI"),[1] which summarizes certain of the Division's views regarding the process by which the SEC staff reviews and comments on post-effective amendments to registration statements submitted pursuant to Rule 485(a) under the Securities Act of 1933, as amended (the "1933 Act").[2] In the ADI, the SEC staff requests that registrants contact the SEC staff prior to making Rule 485(a) filings raising "unique or particularly novel issues" and, in all instances, respond to SEC staff comments on Rule 485(a) filings at least five business days prior to such filings becoming automatically effective.

BACKGROUND

Rule 485(a) under the 1933 Act provides that a post-effective amendment to a registration statement for an open-end management investment company shall become effective automatically within the timeframe set forth in the Rule, which timeframe depends on the changes being effected and the effective date designated by the registrant.[3]

The SEC staff typically reviews and provides comments on Rule 485(a) filings prior to the effective date of the Rule 485(a) filing. Registrants receiving such comments respond to the SEC staff either orally or in the form of a letter that is filed as correspondence on the SEC's Electronic Data Gathering, Analysis, and Retrieval ("EDGAR") database. It is not unusual for a response letter to be filed simultaneously with a post-effective amendment filed pursuant to Rule 485(b) under the 1933 Act that incorporates, among other things, the SEC staff comments that the registrant has accepted. Registrants may designate that a Rule 485(b) filing become effective immediately upon filing or up to thirty days after filing.

SUMMARY

In the ADI, the SEC staff asks registrants to adopt two practices, neither of which is explicitly or implicitly required by Rule 485(a):

1. the SEC staff "urges" registrants to contact the SEC staff prior to making Rule 485(a) filings that "may raise material questions of first impression — or that address issues in a manner inconsistent with previous precedent…" for the purpose of discussing those issues; and
2. the SEC staff "requests" that registrants respond to SEC staff comments on any Rule 485(a) filing — including, presumably, one that does not raise material questions of first impression or address issues in a manner inconsistent with previous precedent — no later than five business days before the filing is

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> scheduled to become effective automatically. “In cases where registrants are unable to submit responses to [SEC staff] comments” within the requested timeframe, the SEC staff “requests that registrants file an amendment under [R]ule 485(b)(1)(iii) delaying the effectiveness date of the filing as needed until [SEC staff] comments have been resolved.”

The ADI states that “seeking automatic effectiveness can complicate efforts by the [SEC staff]…to effectively address investor protection interests,” particularly when filings “raise complex issues not easily resolved because of a lack of precedent.” The ADI lists as examples of issues that “typically” require additional review and interaction between SEC staff and registrants: (1) novel investment strategies; (2) novel fee structures; and (3) novel operational policies (*e.g.*, significant changes to policies related to purchases and redemptions by investors). According to the SEC staff, the practices requested in the ADI “allow both the [SEC staff] and registrants to completely and effectively consider the issues raised and assure a review of amendments in a manner that assists registrants in meeting their timing expectations.”

IMPLICATIONS

As a threshold matter, it is important to emphasize that a registrant has no legal mandate to comply with the ADI requests. In fact, the ADI was released months after the issuance of a public statement by SEC Chair Jay Clayton on September 13, 2018, which highlighted the SEC's “longstanding position…that all [SEC staff] statements are nonbinding and create no enforceable legal rights or obligations of the [SEC] or other parties.” Consistent with Chair Clayton's public statement, the statements in the ADI are expressed as requests rather than mandates, and the ADI states that it represents the SEC staff's views and is not a rule, regulation, or statement of the SEC. Nevertheless, the SEC staff is charged with the day-to-day oversight of registrants and their regulatory filings. Thus, it would be prudent for registrants to consider the SEC staff's views regarding filing procedures. Accordingly, registrants will need to carefully consider whether and how to comply with the ADI requests.

Implications of Complying with the ADI Requests

A registrant will need to consider the legal and business implications attendant to complying with the ADI requests. A registrant that chooses to comply with the ADI requests may need to adjust its Rule 485(a) filing timelines and procedures. After making the determination that a particular post-effective amendment must be submitted pursuant to Rule 485(a), a registrant would then need to determine whether that filing raises material questions of first impression or addresses issues in a manner inconsistent with previous precedent. Although the ADI includes examples of issues that might cause Rule 485(a) filings to fit into these categories, the standard may be difficult to apply to the substance of any particular Rule 485(a) filing. For example, a registrant may have difficulty in determining whether a change in a fund's investment strategy is “novel” or what the SEC staff might view as applicable “previous precedent.”

A registrant that decides to discuss potential issues with the SEC staff prior to submitting a Rule 485(a) filing may wish to build additional time for these discussions into the beginning of its filing timeline, particularly if it is important for the Rule 485(a) filing to become effective on a particular date. Failure to account for any back-and-forth that may result from preliminary discussions with the SEC staff could cause a registrant to make a Rule 485(a) filing later than planned, thus pushing back the earliest date on which the Rule 485(a) filing can become automatically effective. It is unclear what, if anything, the SEC staff may request of the registrant in the course of discussions that precede the submission of a Rule 485(a) filing. The SEC staff could seek to proscribe specific

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disclosure and the underlying strategies or operations described by that disclosure or otherwise indicate disapproval of the registrant's proposed course of action. In that event, a registrant would need to consider whether it wishes to address the SEC staff's concerns prior to filing and how to address any disagreements with the SEC staff, notwithstanding the fact that the registrant is permitted by Rule 485(a) to file a post-effective amendment that becomes effective automatically without explicit SEC staff approval. A registrant that endeavors to address any SEC staff comments or concerns prior to submitting a Rule 485(a) filing might need more time to address those comments or concerns than is contemplated by its filing timeline. Therefore, even when a registrant's filing timeline contemplates a period of time for preliminary discussions with the SEC staff, it is possible that these preliminary discussions will unexpectedly delay or otherwise alter the registrant's plans.

Once a registrant has made a filing pursuant to Rule 485(a), adherence to the ADI requests would entail responding to SEC staff comments on the Rule 485(a) filing at least five business days prior to the designated effective date of the filing.[4] We are aware that certain members of the SEC staff have begun to include this ADI request in the comments that they provide in connection with their review of Rule 485(a) filings. A registrant will need to incorporate into their filing timeline this requested deadline for responding to SEC staff comments. The ADI seems to indicate that the SEC staff might use the five business-day period between a registrant's response to SEC staff comments and the effective date of a Rule 485(a) filing to consider and discuss the registrant's responses to SEC staff comments.[5] As with the process of engaging in a discussion with the SEC staff prior to submitting a Rule 485(a) filing, a registrant receiving feedback from the SEC staff during the five business-day period would need to determine how to deal with disagreements with the SEC staff. It is not uncommon for registrants to respectfully decline to accept SEC staff comments on a Rule 485(a) filing. Entering into a discussion with the SEC staff regarding the reasons for declining would add an additional step to the filing process and, depending on the nature of the discussions, could result in additional delays in making a Rule 485(a) filing effective. Many registrants print summary prospectuses and/or prospectuses in the weeks leading up to the effective date of a Rule 485(a) filing. If the SEC staff's review of a registrant's response to SEC staff comments causes the SEC staff to request additional disclosure changes, those registrants will need to consider how to balance the ADI requests with pre-established printing timelines. Many registrants encounter increased costs when deadlines for submitting final documents to a printing vendor are not met.

In addition, adherence to the ADI requests would require registrants that do not respond to SEC staff comments at least five business days prior to the desired effective date of the Rule 485(a) filing to delay the effective date of the Rule 485(a) filing by making a filing pursuant to Rule 485(b)(1)(iii).[6] This could create a conflict for registrants that must make a Rule 485(a) filing effective on a particular date, such as an annual update to a registration statement that updates a fund's financial information.[7] It could also lead to business impediments in cases where an investor plans to invest in a new fund or share class on a particular date or when a shell fund is being registered to adopt a target fund on a particular date. A change to the effective date of a Rule 485(a) filing could result in disclosure changes triggered by additional SEC staff comments and may require a change to the date of the prospectus, either of which may affect a registrant's printing schedule. Registrants will need to balance the ADI request for delays in effectiveness with these legal and business considerations.

Implications of Not Complying with the ADI Requests

Not complying with the ADI requests risks complicating a registrant's relationship with the SEC staff. For example, a registrant seeking acceleration of the effective date of a Rule 485(a) filing pursuant to Rule 461 under the 1933

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Act will need the SEC staff to affirmatively issue an order declaring the Rule 485(a) filing effective. The SEC staff may be less cooperative in granting such an order if the registrant has a prior history of failing to comply with the ADI requests.

Not complying with the ADI requests also could result in heightened scrutiny with respect to SEC staff review of disclosure documents, particularly if a reviewer is familiar with the registrant's practice of not complying with the ADI requests. This heightened scrutiny could lead to instances where the SEC staff determines that a registration statement includes materially misleading misstatements and omissions. This is particularly true because, by engaging in discussions with the SEC staff, whether prior to submitting a Rule 485(a) filing or after responding to SEC staff comments on a Rule 485(a) filing, a registrant may gain access to valuable observations and insights regarding particular disclosure issues or industry trends. A registrant that does not comply with the ADI requests may not have access to these observations and insights to the same extent. In this way, discussions with the SEC staff in adherence to the ADI requests could reduce the possibility that a registrant's registration statement or post-effective amendment thereto conflicts with SEC staff guidance or interpretations. If the SEC staff determines that a registration statement includes materially misleading misstatements and omissions, it could seek to bring an enforcement action under the anti-fraud provisions of applicable federal securities laws or other provisions of those laws relating to disclosure requirements.

Additionally, while the issuance of stop orders is extraordinarily rare, especially with respect to mutual fund registration statements, the SEC is empowered to issue stop orders under Section 8(d) of the 1933 Act, if the SEC finds that a registration statement “includes any untrue statement of a material fact or omits to state any material fact required to be stated therein or necessary to make the statements therein not misleading.” Section 8(e) of the Investment Company Act of 1940, as amended (the “1940 Act”), grants similar power to the SEC with respect to registration statements filed under the 1940 Act. A stop order can be issued either prior to or after the effective date of a registration statement or a post-effective amendment thereto. We are not aware of the SEC having issued a stop order with respect to a mutual fund registration statement in the last several decades. However, discussions with the SEC staff in adherence to the ADI requests could reduce the already unlikely possibility that a registrant's registration statement or post-effective amendment thereto meets the applicable standards for issuing stop orders.

CONCLUSION

Registrants will need to balance the potential benefits of complying with the ADI requests against the potential burdens that the ADI requests might impose with respect to each Rule 485(a) filing. The ADI was posted on the “Disclosure” webpage on the Division's website, which the SEC staff has used to post Accounting and Disclosure Information releases and other forms of SEC staff guidance regarding disclosure issues. It appears that the SEC staff continues to periodically convey its views on disclosure matters by updating this webpage. Therefore, registrants may wish to monitor this webpage on an ongoing basis for further SEC staff statements, in whatever form they may be issued. The “Disclosure” webpage on the Division's website can be found at https://www.sec.gov/investment/fund-disclosure-at-a-glance.

NOTES

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[1] According to the SEC's Disclosure Review and Accounting Office, Accounting and Disclosure Information releases are intended to aid “practitioners and others who are interested in the law and interpretations concerning disclosure.” Nevertheless, each Accounting and Disclosure Information release includes a prominent statement that the release represents the views of the Division and that the SEC has neither approved nor disapproved of the content of the release. The Division has issued seven Accounting and Disclosure Information releases in total, the first six of which were all issued on June 12, 2018.

[2] ADI 2019-07 - Review of Certain Filings Under Automatic Effectiveness Rules, *available at* https://www.sec.gov/investment/accounting-and-disclosure-information/adi-2019-07-review-certain-filings-under-automatic.

[3] Pursuant to Rule 485(a), a filing shall become effective automatically between sixty and eighty days after the date on which the amendment is filed, except that a post-effective amendment that is filed for the purpose of adding a series shall become effective between seventy-five and ninety-five days after the date on which the amendment is filed. A registrant can designate any date that falls within the timeframe provided by the Rule as the date on which the filing will become effective.

[4] This ADI request assumes that SEC staff comments are provided sufficiently in advance of the designated effective date of a Rule 485(a) filing to enable a registrant to process and respond to SEC staff comments no later than five business days prior to that designated effective date.

[5] For example, the ADI states that, in the SEC staff's experience, the practices requested in the ADI “allow both the [SEC staff] and registrants to completely and effectively consider the issues raised and assure a review of amendments in a manner that assists registrants in meeting their timing expectations.”

[6] The ADI does not specify the number of days by which the effective date of a post-effective amendment should be extended, but instead requests that, under these circumstances, the effective date be delayed “as needed until [SEC staff] comments have been resolved.” Read literally, compliance with this ADI request could require registrants to delay the effective date of a Rule 485(a) filing indefinitely until SEC staff comments have been resolved. However, the ADI does not request such indefinite delays in cases where a registrant provides responses to SEC staff comments at least five business days prior to the date on which a Rule 485(a) filing becomes effective. Therefore, it would be reasonable to assume that a registrant has satisfied the ADI request if it delays a Rule 485(a) filing by the number of days necessary to provide five business days between the date that a registrant responds to SEC staff comments and the date that the Rule 485(a) filing becomes automatically effective. Any other reading of the ADI request would mark a significant departure from the current SEC staff comment process, which involves filings becoming automatically effective even if a registrant respectfully declines to accept one or more SEC staff comments, thus rendering those comments potentially “unresolved.” The SEC staff is typically only in a position to require a registrant to accept all of the SEC staff's comments when a registrant has requested that the SEC staff accelerate the effective date of a post-effective amendment pursuant to Rule 461 under the 1933 Act or when a registrant is requesting that the SEC staff declare an initial registration statement effective pursuant to Section 8(a) of the 1933 Act.

[7] Section 10(a)(3) of the 1933 Act prohibits continuously offered investment companies from using a registration statement with financial information that is more than 16 months old.

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