

MEMO# 35925

November 13, 2024

SEC Division of Investment Management Issues ADI 2024-14: Tailored Shareholder Report Common Issues

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TO: ICI Members
Accounting/Treasurers Committee
Chief Compliance Officer Committee
Operations Committee
Small Funds Committee
Transfer Agent Advisory Committee
SUBJECTS: Compliance
Disclosure
Fees and Expenses
Fund Accounting & Financial Reporting
Operations RE: SEC Division of Investment Management Issues ADI 2024-14: Tailored
Shareholder Report Common Issues

On November 7th, the Securities and Exchange Commission's (SEC) Division of Investment Management Disclosure Review and Accounting Office (DRAO) issued Account and Disclosure Information 2024-14^[1] (the ADI) to address common issues observed in the implementation of the SEC's new requirements for mutual funds and exchange-traded funds (ETFs) to prepare and transmit concise, visually engaging shareholder reports (tailored shareholder reports). These changes, effective July 24, 2024, apply to all funds registered on Form N-1A and are aimed at providing retail investors with clearer and more relevant information regarding fund performance, expenses, and portfolio holdings.

The Division of Investment Management, through DRAO, is responsible for overseeing fund disclosures, including tailored shareholder reports. The ADI notes that DRAO has identified several recurring issues in the implementation of the new requirements for these reports. The purpose of the ADI is to remind funds of key compliance requirements, flag common issues, and suggest best practices to ensure a smooth transition to these new disclosure standards. The ADI also reminds the industry that the SEC staff has provided frequently asked questions (FAQs)^[2] on tailored shareholder reports, which are available on the SEC's website, and states that the SEC staff will continue to update the guidance as needed.

Key Takeaways:

1. Expense Information:

- Funds must present simplified expense data for annual and semi-annual reports in a specific format. See Item 27A(c) of Form N-1A. Issues identified include:
 - Funds incorrectly annualizing, in semi-annual reports, expenses in dollars paid on a \$10,000 investment (See Instruction 2(c) to Item 27A(c))
 - Funds incorrectly calculating the expenses in dollars paid on a \$10,000 investment by multiplying the "costs paid as a percentage of your investment" by \$10,000 instead of by the average account value over the period (See Instruction 2(a) to Item 27A(c))
 - Funds incorrectly presenting expenses to the nearest cent instead of rounding to the nearest dollar (See Instruction 1(a) to Item 27A(c))
- The ADI also suggests that funds "consider noting in their semi-annual reports that costs paid as a percentage of a \$10,000 investment is an annualized figure."

2. Management's Discussion of Fund Performance (MDFP):

- Funds must include a performance table showing average annual returns for the 1-, 5-, and 10-year periods, with performance based on a fund's net asset value. DRAO has observed that many ETFs also disclose performance based on a fund's market value. The ADI states that ETFs should only present performance based on net asset value, not market value. (See Instruction 3 to Item 27A(a) and Instruction 5 to Item 27A(d)(2))
- Funds must compare performance to an appropriate broad-based securities market index, and DRAO reminds funds to avoid using specialized or narrow indexes.
- Funds must include a statement that past performance is not a good predictor of the fund's future performance, and DRAO reminds funds to use text features to make the statement noticeable and prominent. (See Item 27A(d)(2)(iii)(A))

3. Fund Statistics:

- Some funds have incorrectly presented portfolio-related statistics (e.g., average maturity, credit rating) in the wrong section of the report. The ADI states that these should be categorized under "Fund Statistics" rather than under "Graphical Representation of Holdings." (See Item 27A(e))

4. Graphical Representation of Holdings:

- Funds must categorize their holdings using one or more tables, charts or graphs depicting the fund's portfolio holdings by category, and funds must disclose the basis for their percentages (i.e., whether the percentage is based on net asset value, total investments, total exposure, or net exposure attributable to each category). (See Item 27A(f)) The DRAO staff has noted instances where funds have not disclosed the basis for the percentage.
- If a fund categorizes its holdings based on credit quality, the fund is required to include certain special disclosures. (See Item 27A(f)). The ADI notes that some funds have not provided the required special disclosures.
- The ADI further suggests that funds "consider selecting categories that are most helpful for investors to assess and monitor their fund investments."

5. Material Changes:

- Funds are required to include disclosures of material changes that have occurred since the start of the reporting period. The DRAO staff has observed that some funds

with material changes failed to include the necessary cover page disclosure, and that, conversely, some funds included the cover page disclosure but omitted the disclosures of material changes themselves. (See Items 27A(b)(5) and 27A(g))

6. Availability of Additional Information Online:

- Funds must ensure that links to additional information on their websites work properly and direct investors to the specific required disclosures, rather than a home page or a section of the fund's website other than on which the information is posted. The ADI notes that broken links and links that are not specific enough have been recurring issues. The ADI also reminds funds to make all required information publicly accessible, free of charge.
- The ADI further suggests that funds "consider referring to [Form N-CSR Item 7-11 information on the funds' websites] by a term that is more descriptive of the collective information required by Items 7-11 of Form N-CSR." As an example, the ADI suggests referring to the information as "Annual Financial Statements and Additional Information."

7. Inline XBRL Data Tagging:

- The ADI notes that some funds have incorrectly tagged additional indexes as broad-based indexes.

8. General Reporting Issues:

- DRAO reminds funds to avoid including extraneous disclosures (such as lengthy disclaimers or risk disclosures) not required or permitted under Form N-1A (See Instruction 3 to Item 27A(a)), and to adhere to the prescribed order of disclosures in Item 27A. (See Instructions 1 ad 2 to Item 27A(a))
- Funds are also reminded that they may omit inapplicable disclosures (such as material fund changes or changes in and disagreements with accountants). (See Instruction 7 to Item 27A(a))

Conclusion:

The ADI encourages funds to carefully review their shareholder reports and associated website disclosures to ensure compliance with SEC regulations under rule 30e-1 of the Investment Company Act, Form N-1A and Form N-CSR.

For further clarification or questions, feel free to reach out to the undersigned, or the SEC's Division of Investment Management's Disclosure Review and Accounting Office (DRAO) is available at IMDRAO@sec.gov.

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Notes

[1] See ADI-2024-14: Tailored Shareholder Report Common Issues, SEC Division of Investment Management (last updated Nov. 8, 2024), available at [tsr-adi-11-6-2024.pdf](#).

[2] See Tailored Shareholder Reports Frequently Asked Questions, [SEC Division of Investment Management \(last updated Jan. 26, 2024\)](#), available at <https://www.sec.gov/investment/tailored-shareholder-reports-faqs>.

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