

## SEC Updates N-PORT & N-CEN Reports for Funds

On August 28, 2024, the SEC voted 3-2 to issue a final rule requiring monthly reporting of fund portfolio holdings by registered open-end funds, registered closed-end funds, and exchange-traded funds organized as a unit investment trust. Open-end funds also would be required to disclose details on service providers used for liquidity risk management. In response to feedback, the SEC dropped more extensive changes that included swing pricing, public reporting of liquidity classifications, and increased frequency of Regulation S-X compliant portfolio information.<sup>1</sup>



### N-PORT New Disclosures & Monthly Reporting

Form N-PORT requirements were initially adopted in 2016 and funds would have been required to file monthly reports within 30 days of month-end. However, due to concerns about the strength of the SEC’s cybersecurity protections, the initial N-PORT reporting was postponed. In 2019, the SEC adopted an interim final rule requiring registered management investment companies to file a report on Form N-PORT for each month in a fiscal quarter within 60 days of quarter-end with details about portfolio holdings. The public has access to certain information for the third month of each quarter.

Under the final rule, all registered investment companies that report on Form N-PORT would be required to file Form N-PORT **monthly within 30 days of month-end**, and reports would be publicly available 60 days after month-end.

There are no changes to the information on Form N-PORT that is currently nonpublic, e.g., liquidity classifications for individual portfolio investments, derivative transactions, and miscellaneous securities. However, the SEC may publish aggregate or other anonymized information about the nonpublic elements of Form N-PORT.

For commentators concerned about predatory trading based on public information, the SEC notes that Form N-PORT allows a fund to treat an instrument as a miscellaneous security for up to one year if the position does not exceed 5% of the fund and has not been previously disclosed to the public.

The SEC estimates that as of December 31, 2023, there are 12,561 funds that currently file reports on Form N-PORT holding almost \$30 trillion in assets.

### N-CEN Liquidity Service Provider Information

The Form N-CEN amendments will require open-end funds that are subject to liquidity risk management program requirements under Rule 22e-4 under the *Investment Company Act of 1940* (the Liquidity Rule) to report the following information about service providers used to fulfill Liquidity Rule requirements:

- Name each liquidity service provider

<sup>1</sup>The SEC may consider re-exposing these changes as a separate project.  
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- Provide identifying information, including the legal entity identifier—if available—and location for each liquidity service provider
- Identify if the liquidity service provider is affiliated with the fund or its investment adviser
- Identify the asset classes for which that liquidity service provider provided classifications
- Indicate whether the service provider was hired or terminated during the reporting period

The SEC notes that as of December 31, 2023, 2,749 registered investment companies file reports on Form N-CEN of which 1,257 have funds that are subject to the Liquidity Rule.

## Liquidity Risk Management Program Guidance

The November 2022 proposal had substantial changes to the Liquidity Rule, including stress testing, changes to the liquidity categories, daily liquidity classification, and a minimum 10% holdings of highly liquid assets. All these items were dropped from the final rule. Instead, the SEC provides additional guidance on classification frequency, definition of cash, and highly liquid investment minimums.

### Current Guidance

The Liquidity Rule requires open-end funds to adopt and implement liquidity risk management programs, including:

- Assessment, management, and periodic review of a fund's liquidity risk
- Classification of the liquidity of each of a fund's portfolio investments into one of four prescribed categories and at-least-monthly classification reviews
- Determination and periodic review of a highly liquid investment minimum for certain funds
- Limitation on illiquid investments
- Board oversight

The liquidity classifications of holdings must be reported at least monthly on Form N-PORT. The four liquidity categories are based on the number of days the investment could reasonably be converted into cash or sold without significantly changing its market value—highly liquid, moderately liquid, less liquid, and illiquid. Funds must have a minimum level of highly liquid investments and a 15% maximum limit on illiquid investments. Funds have discretion in determining this classification; investments can be classified individually or by asset class and the asset class composition can be determined by the fund.

A fund must immediately report to the fund's board and on Form N-RN if the portfolio becomes more than 15% illiquid, or if a fund breaches the minimum highly liquid investment level established as part of its liquidity risk management program for seven consecutive days.

### Frequency of Classification

Under the final rule, funds must review liquidity classifications more frequently than monthly if changes in market, trading, and investment-specific considerations are reasonably expected to materially affect one or more of the fund's investment classifications. Funds must adopt and implement policies and procedures reasonably designed to conduct the required intra-month review of liquidity classifications when such events occur. These policies and procedures should identify the type of information a fund will use to identify relevant intra-month changes and to review liquidity classifications intra-month, as well as the timeliness of that information. If a fund lacks information or uses stale information, it may not be able to identify when intra-month reviews of liquidity classifications are required.

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In outreach, the SEC has observed certain funds were not prepared to review classifications intra-month in response to changing conditions. This final rule re-emphasizes several considerations for intra-month classification included in the 2016 Liquidity Rule:

- Marketwide developments:
  - Changes in interest rates or other macroeconomic events
  - Marketwide volatility
  - Marketwide flow changes
  - Dealer inventory or capacity changes
  - Extraordinary events such as natural disasters or political upheaval
- Asset-class and investment-specific developments:
  - Regulatory changes affecting certain asset classes and corporate events (such as bankruptcy, default, pending restructuring, or delisting, as well as reputational events)

The SEC now advises that funds generally also should consider reviewing liquidity classifications if **changes in portfolio composition** are reasonably expected to materially affect one or more investment classifications. For example, if a fund substantially increases the size of an investment position, the total holding may adversely affect the liquidity classification if the market depth makes it difficult to sell the investment within a particular time frame without causing a significant market value change.

Funds also should consider classifying investments intra-month if a newly acquired investment is reasonably expected to result in material changes to the fund's liquidity profile if the changes to the fund's liquidity profile may cause a shortfall below a fund's highly liquid investment minimum or cause the fund to exceed the limit on illiquid investments.

## Cash

To determine whether an investment can be classified as highly liquid or moderately liquid, a fund must consider the time it reasonably expects an investment to be convertible to cash without significantly changing the investment's market value. "Cash" in the Liquidity Rule means U.S. dollars and does not include foreign currencies or cash equivalents.

The SEC has observed some international funds considering the time in which an investment would be convertible to a different currency other than U.S. dollars as the relevant period for determining when an investment is convertible to cash, even though the funds pay cash redemptions in U.S. dollars. SEC examinations also have revealed that some funds are classifying any currency as a highly liquid investment, regardless of the time frame to convert that currency to U.S. dollars.

A fund should consider the amount of time it is reasonably expected to take to convert a reasonably anticipated trade size of that currency into U.S. dollars under current market conditions without significantly changing the currency exchange rate. Relevant factors include the presence of currency controls, the presence of an active market in forward or spot contracts exchanging the currency for U.S. dollars, and any delays in currency conversions driven by market structure or operations.

Funds should not base liquidity determinations in an international jurisdiction on the ability to sell, dispose of, or settle an investment into the local currency without also considering the ability to convert the local currency into U.S. dollars.

The final rule notes **if a fund does not reasonably expect to be able to convert the local currency into U.S. dollars within seven calendar days because of currency controls or otherwise, then the local currency should be classified as an illiquid investment. Other investments in that jurisdiction that would be sold or disposed of in exchange for the illiquid local currency also should be classified as illiquid investments.**

## Highly Liquid Investment Minimums

The highly liquid investment minimum requirement is intended to increase the likelihood that a fund will be able to meet redemptions without significant dilution for remaining fund investors. For funds with portfolios that are on the lower end of the liquidity spectrum, the SEC reiterates the importance of a highly liquid investment minimum that considers a fund's particular risk factors.

“When considering a fund's investment strategy and portfolio liquidity, a fund that invests significantly in less liquid or illiquid investments, such as a bank loan fund, generally should consider establishing a highly liquid investment minimum that is higher than that of a fund that is more liquid. Funds with investment strategies that have had greater volatility of flows than other investment strategies—or that are reasonably expected to have greater volatility in reasonably foreseeable circumstances—would generally need highly liquid investment minimums that are higher than funds whose strategies tend to entail less flow volatility.

While a line of credit or similar arrangement can facilitate a fund's ability to meet unexpected redemptions and can be taken into consideration when determining its highly liquid investment minimum, we continue to believe that liquidity risk management is better conducted primarily through construction of a fund's portfolio.”

The liquidity rule does not mandate how a portfolio manager should meet redemptions. A fund is not required to only—or primarily—use its most liquid investments to meet redemptions.

“The requirement does not mean that a fund must continuously maintain a specific level of highly liquid assets and cannot use those assets to meet redemptions.”

## Conclusion

The asset management team at Forvis Mazars 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 Mazars as a top 25 accounting and audit firm to registered investment advisors. Forvis Mazars also was 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 [forvismazars.us](https://forvismazars.us).

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