



441 G St. N.W.
Washington, DC 20548

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December 31, 2020

The Honorable Mike Crapo
Chairman
The Honorable Sherrod Brown
Ranking Member
Committee on Banking, Housing, and Urban Affairs
United States Senate

The Honorable Maxine Waters
Chairwoman
The Honorable Patrick McHenry
Ranking Member
Committee on Financial Services
House of Representatives

Subject: *Securities and Exchange Commission: Use of Derivatives by Registered Investment Companies and Business Development Companies*

Pursuant to section 801(a)(2)(A) of title 5, United States Code, this is our report on a major rule promulgated by the Securities and Exchange Commission (the Commission) entitled “Use of Derivatives by Registered Investment Companies and Business Development Companies” (RIN: 3235-AL60). We received the rule on December 14, 2020. It was published in the *Federal Register* as a final rule on December 21, 2020. 85 Fed. Reg. 83162. The effective date of this final rule is February 19, 2021.

According to the Commission it is adopting a new exemptive rule under the Investment Company Act of 1940 (the “Investment Company Act”), designed to address the investor protection purposes and concerns underlying section 18 of the Investment Company Act and to provide an updated and more comprehensive approach to the regulation of funds’ use of derivatives and the other transactions the new rule addresses. *See generally* 15 U.S.C. § 80a–18. The Commission stated, it is adopting new reporting requirements designed to enhance its ability to effectively oversee funds’ use of and compliance with the new rule, and to provide the Commission and the public additional information regarding funds’ use of derivatives. The Commission also stated that it is adopting amendments under the Investment Company Act to allow leveraged/inverse exchange-traded funds that satisfy the rule’s conditions to operate without the expense and delay of obtaining an exemptive order. The Commission stated further, it is rescinding certain exemptive relief that has been granted to these funds and their sponsors.

Enclosed is our assessment of the Commission's compliance with the procedural steps required by section 801(a)(1)(B)(i) through (iv) of title 5 with respect to the rule. If you have any questions about this report or wish to contact GAO officials responsible for the evaluation work relating to the subject matter of the rule, please contact Shari Brewster, Assistant General Counsel, at (202) 512-6398.

A handwritten signature in black ink that reads "Shirley A. Jones". The signature is written in a cursive, flowing style.

Shirley A. Jones
Managing Associate General Counsel

Enclosure

cc: Vanessa Countryman
Secretary
Securities and Exchange Commission

REPORT UNDER 5 U.S.C. § 801(a)(2)(A) ON A MAJOR RULE
ISSUED BY THE
SECURITIES AND EXCHANGE COMMISSION
ENTITLED
“USE OF DERIVATIVES BY REGISTERED INVESTMENT
COMPANIES AND BUSINESS DEVELOPMENT COMPANIES”
(RIN: 3235-AL60)

(i) Cost-benefit analysis

The Securities and Exchange Commission (the Commission) provided an analysis of the cost and benefits of this final rule. According to the Commission, this analysis includes both qualitative assessments and quantified estimates of the economic effects, including the initial and ongoing costs of the additional reporting requirements, where feasible. The Commission discussed the cost and benefits of the final rule as it relates to the following: (1) Derivatives Risk Management Program and Board Oversight and Reporting; (2) VaR-Based Limit on Fund Leverage Risk; (3) Limited Derivatives Users; (4) Reverse Repurchase Agreements and Similar Financing Transactions; (5) Treatment of Existing Leveraged/Inverse Funds That Seek To Provide Leveraged or Inverse Market Exposure Exceeding 200 Percent of the Return of the Relevant Index; (6) Amendments to Rule 6c-11 Under the Investment Company Act and Rescission of Exemptive Relief for Leveraged/Inverse Exchange-Traded Funds; (7) Unfunded Commitment Agreements; (8) Recordkeeping; (9) Amendments To Fund Reporting Requirements; and (10) When-Issued and Forward-Settling Transactions.

(ii) Agency actions relevant to the Regulatory Flexibility Act (RFA), 5 U.S.C. §§ 603-605, 607, and 609

The Commission prepared a Final Regulatory Flexibility Analysis. The analysis included: (1) the need for and objectives of this final rule and form amendments; (2) significant issues raised by public comments; (3) small entities subject to the final rule; (4) projected reporting, recordkeeping, and other compliance requirements; and (5) agency action to minimize effect on small entities.

(iii) Agency actions relevant to sections 202-205 of the Unfunded Mandates Reform Act of 1995, 2 U.S.C. §§ 1532-1535

As an independent regulatory agency, the Commission is not subject to the Act. See 2 U.S.C. §§ 658(1), 1502(1).

(iv) Other relevant information or requirements under acts and executive orders

Administrative Procedure Act, 5 U.S.C. §§ 551 *et seq.*

On January 24, 2020, the Commission issued a proposed rule. *Use of Derivatives by Registered Investment Companies and Business Development Companies; Required Due*

Diligence by Broker-Dealers and Registered Investment Advisers Regarding Retail Customers' Transactions in Certain Leveraged/Inverse Investment Vehicles, Investment Company Act, 85 Fed. Reg. 4446. The Commission received approximately 6,100 comments and addressed these comments throughout the preamble of this final rule.

Paperwork Reduction Act (PRA), 44 U.S.C. §§ 3501-3520

The Commission determined that this final rule contains information collection requirements under the Act. The Commission stated that it submitted the information collection requirements to the Office of Management and Budget (OMB) for review. The Commission noted the titles for the existing information collections affected by the final rule are: "Form N-PORT" (OMB Control Number 3235-0731); "Rule 30b1-10 and Form N-LIQUID" (OMB Control Number 3235-0754); "Form N-CEN" (OMB Control Number 3235-0730); and "Rule 6c-11 under the Investment Company Act of 1940, Exchange-traded funds" (OMB Control Number 3235-0764). The Commission also noted that the title of the new information collection will be, "Rule 18f-4 under the Investment Company Act of 1940, Use of Derivatives by Registered Investment Companies and Business Development Companies." The Commission estimated the burden of each ICR.

Statutory authorization for the rule

The Commission promulgated this final rule pursuant to sections, 77c, 77f, 77g, 77h, 77j, 77s, 77z-2, 77z-3, 77sss, 78c, 78l, 78m, 78n, 78o(d), 78o-7 note, 78u-5, 78w(a), 78ll, 78mm, 80a-2(a), 80a-3, 80a-8, 80a-9, 80a-10, 80a-13, 80a-24, 80a-26, 80a-29, 80a-30, and 80a-37 of title 15, United States Code; and section 107 of the Jumpstart Our Business Startups Act, Public Law 112-106.

Executive Order No. 12866 (Regulatory Planning and Review)

As an independent regulatory agency, the Commission is not subject to the Order.

Executive Order No. 13132 (Federalism)

As an independent regulatory agency, the Commission is not subject to the Order.