

December 22, 2020

Vanessa A. Countryman
Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

Re: Tailored Shareholder Reports, Treatment of Annual Prospectus Updates for Existing Investors, and Improved Fee and Risk Disclosure for Mutual Funds and Exchange-Traded Funds; Fee Information in Investment Company Advertisements (File No. S7-09-20)

Dear Ms. Countryman:

The Vanguard Group Inc. (Vanguard)¹ supports the Securities and Exchange Commission's (the Commission) proposal to modernize disclosure for open-end management investment companies (the Proposal)² by introducing a concise and visually engaging disclosure framework that provides investors with timely access to key information. Like the Commission, Vanguard has been an enduring advocate of disclosure modernization and improving the fund investor experience on behalf of the more than 30 million investors who invest in Vanguard funds. As an investment adviser with more than four decades of experience, we appreciate how effective disclosure empowers investors to make informed investment decisions. Over the past several years, it has become increasingly apparent that retail investors prefer clear and concise disclosure documents that they can access electronically, and that highlight the most relevant information necessary to assess and monitor their investments. We believe the COVID-19 crisis faced by U.S. investors and fund sponsors this year reinforces and makes more urgent the need for electronic delivery of Commission-required disclosures to investors. Our comments aim to highlight areas that would further align the Proposal with these disclosure preferences.

Electronic delivery lies at the core of a modern, effective disclosure framework. We strongly believe the Commission should treat electronic delivery as the equivalent to paper delivery and

¹ Vanguard is one of the world's leading asset managers. As of October 31, 2020, Vanguard managed approximately \$6.3 trillion in assets globally on behalf of more than 30 million investors. Vanguard's core purpose is to take a stand for all investors, to treat them fairly, and to give them the best chance for investment success.

² Tailored Shareholder Reports, Treatment of Annual Prospectus Updates for Existing Investors, and Improved Fee and Risk Disclosure for Mutual Funds and Exchange-Traded Funds; Fee Information in Investment Company Advertisements, 85 Fed. Reg. 70716 (November 5, 2020), *available at* <https://www.govinfo.gov/content/pkg/FR-2020-11-05/pdf/2020-17449.pdf>.

allow funds to use electronic delivery as the default communication method. Access to product information online and digital communications between consumers and companies are becoming foundational service expectations in numerous industries, including financial services. Data shows that mutual fund investors increasingly utilize the internet to access fund information and prefer digital communications.³ Expanding the availability of electronic delivery would comport with investors' preference to access disclosure on their terms. Additionally, permitting electronic delivery as a default communication method would appropriately recognize that advancements in technology can simultaneously improve the investor experience and reduce costs. Of course, any rule permitting electronic delivery should ensure that investors that prefer to receive paper communications will have their preference honored.

Our comments also address the proposed content of mutual fund disclosures. We applaud the Commission's efforts to increase consistency and transparency in fee and expense disclosures, including advertising materials. Although we welcome the Proposal and support the Commission's effort to improve the investor experience by modernizing mutual fund disclosures, we recommend certain changes to the proposed framework that we believe will better serve investors in the long term and enhance the investor experience overall. Specifically, we recommend that the Commission:

- Take a principles-based approach to a number of disclosure requirements in the Proposal, including descriptions of material fund changes, principal risk disclosure, and liquidity risk management program disclosure;
- Allow fund complexes to retain the ability to include multiple funds in a single shareholder report where appropriate; and
- Adjust certain provisions within the Proposal to address their operational feasibility and effects they may have on the industry.

I. Electronic Delivery of Fund Documents

We urge the Commission to treat electronic delivery as equal to paper delivery throughout the Federal securities laws, including permitting electronic delivery to be the default communication method for all fund disclosure documents. At a minimum, the Commission should retain Rule 30e-3 as an option for open-end funds to continue to use a notice and access framework to satisfy delivery of shareholder reports.

A. The Commission Should Permit Electronic Delivery of Fund Documents as a Default Communication Method To Reflect Investor Preference and Improve Disclosure for Fund Shareholders While Preserving Investor Protections

We strongly urge the Commission to expand availability of electronic delivery by treating electronic delivery as equal to paper delivery throughout the Federal securities laws and by

³ Since at least 2015, Vanguard has seen year over year increases in investors who sign up for electronic delivery of fund disclosure documents. During the second quarter of 2020, those increases were between 12–17% in various distribution channels.

leveraging technology to reduce expenses borne by fund shareholders.⁴ Historically, the Commission's rules on mutual fund disclosure have privileged paper delivery by prohibiting funds from satisfying disclosure delivery standards electronically, unless a shareholder affirmatively consents to receiving electronic disclosure. The Commission took an important step toward modernizing its disclosure practices in 2018 when it adopted Rule 30e-3 under the Investment Company Act of 1940, which creates an optional notice and access framework to satisfy delivery of shareholder reports.

Amending the scope of Rule 30e-3 to exclude open-end funds runs contrary to investor preference for electronic delivery and the evolving manner in which investors are consuming fund data. In our experience, most fund investors demonstrate a behavioral preference for a digital experience. Retail investors, for example, overwhelmingly connect with us through a digital platform, *e.g.*, on the web, or through a mobile device. As of June 2020, approximately 85% of investors onboarding on our new brokerage platform elected to receive fund documents electronically.⁵ In addition, Vanguard has had less than 0.5% of investors contact us to request receipt of printed documents under Rule 30e-3. Investor preference for electronic engagement is not surprising, given the availability of internet access and the significant advantages that electronic communications have compared to paper alternatives.⁶ Websites provide continuous access to disclosure information and enable shareholders to peruse this information from the convenience of their home or mobile device. Compared to electronic delivery, paper delivery is delayed and incapable of providing investors with an interactive experience. Additionally, adoption of an electronic delivery framework for all fund delivery obligations has the potential to reduce fund expenses borne by shareholders.

The specific parameters of an electronic delivery framework should adhere to three principles to ensure that the framework meets investor needs and remains current as technology evolves.

- **Optionality.** To ensure that investor preference remains a guiding principle for the delivery of disclosure documents, the Commission should provide all investors the right to “opt out” of electronic delivery. Although we expect that few shareholders would elect to opt out, those that do would continue to receive paper notices on Commission-prescribed timelines. Electronic delivery would simply have no effect on these shareholders, except that they too would benefit from any reduced fund expenses realized from the increased use of electronic delivery generally.
- **Flexibility.** Any electronic delivery framework should be flexible to permit delivery mechanisms to evolve with changes in technology and the tools fund investors use to

⁴ This view is consistent with our long-standing position that electronic delivery benefits investors. *See* Letter from Anne E. Robinson, General Counsel and Managing Director, The Vanguard Group, Inc. to Brent J. Fields, Secretary, Commission, dated October 31, 2018, *available at* <https://www.sec.gov/comments/s7-12-18/s71218-4593932-176327.pdf>.

⁵ Electronic delivery election by shareholders invested directly in the Vanguard Funds through the transfer agent, however, is approximately 46%.

⁶ Approximately 94% of brokerage clients, and 81% of fund direct investors have provided us with email information.

access digital information (e.g., email address or internet-connected mobile device number).

- **Investor Protection.** The framework should incorporate investor protections such as notice, choice, and safeguards to permit use of an investor's electronic address as the primary address for disclosure delivery. For example, the framework should contemplate reliability standards for the websites that contain fund disclosure documents and procedures for a fund to follow to resolve an invalid or inoperable electronic address such as by sending the electronic communication to a secondary electronic address, obtaining a new electronic address from the investor, or treating the investor as if they opted out of electronic delivery.⁷ Importantly, we believe that actions such as these will help ensure investor protections are preserved under an expanded electronic delivery framework.

For certain fund documents, such as semi-annual shareholder reports and Section 19a notices, we encourage the Commission to consider an electronic delivery framework that would accept access to fund documents online as satisfying delivery requirements. These documents could remain available to shareholders online in recognition of investor trends in consumption of fund data and create cost savings to the fund and its shareholders.

B. The Commission Should Permit Open-End Funds To Continue to Rely on Rule 30e-3

Even if the Commission does not agree that the benefits and reliability of electronic delivery make it an appropriate default option for all fund disclosures, Vanguard urges the Commission to retain Rule 30e-3 as an option for open-end funds to avoid causing investor confusion and imposing additional needless costs on fund shareholders. Many open-end funds will start relying on Rule 30e-3 beginning in January 2021. We believe that rescinding the rule without adopting an alternative framework for electronic delivery will result in confusion for millions of investors. Funds have sent notices to their investors for two years to ensure they are aware of upcoming delivery changes under Rule 30e-3, and we believe these investors would be confused if the Commission requires open-end funds to return to paper delivery.

Additionally, many fund complexes, including Vanguard, have already expended significant resources in preparation for the transition to Rule 30e-3. Rescission of the rule now, or in the near future, will not only confuse investors but may also impact the underlying costs of their fund investments. We strongly believe that expanding electronic delivery is the best path forward, and we are confident that Rule 30e-3 is a step in the right direction that should be maintained.

II. The Commission Should Focus on a Principles-Based Approach to Disclosure Requirements

We support the Commission's efforts to increase consistency and transparency in fee and expense disclosures, including the proposal to provide qualitative descriptions of material

⁷ Notably, in 2020, our data indicated that the percentage of "bounce-backs" received from electronic communications to investors was less than "return to sender" instances in standard mail delivery.

performance expenses, such as securities lending fees, as a footnote to the fee table found in the prospectus.⁸ We also strongly urge the Commission to maintain a focus on a principles-based, rather than prescriptive, approach to disclosure requirements.⁹ A principles-based approach should be used to encourage funds to convey key information to investors in a clear and concise manner. We believe that a few aspects of the Proposal have the potential to, in practice, work against this principle and result in overly technical and lengthy disclosure, increased fund expenses, and decreased investor engagement.

A. Material Fund Changes

We recommend modifications to the Proposal's requirement to describe material changes to items enumerated in Item 27A(g) that occurred since the beginning of the reporting period, or that the fund plans to make in connection with its annual prospectus update.¹⁰ Specifically, we urge the Commission to modify the Proposal to reflect principles-based guidance that encourages consistency across the industry, but also makes clear that the responsibility to determine the materiality of any change in the enumerated sections remains with the fund.¹¹ This principles-based guidance should apply equally to the determination of material changes that result in notices required under proposed Rule 498B.¹² We also urge the Commission to remove the requirement to discuss planned changes in the proposed Summary of Material Changes section of shareholder reports. Finally, we ask that the Commission confirm in any adopting release or guidance that the proposed disclosure amendments are not intended to change the "total mix of information" available to shareholders or affect how courts should assess fund disclosures.

Without these modifications, many fund complexes may include overly long descriptions of fund changes in shareholder reports and determine to send notices for all fund changes, not just material changes, to mitigate a perceived increase in litigation risk. This could also lead to a lower adoption rate of Rule 498B and negate the Proposal's aim to provide investors with concise information.

B. Risk Disclosures

⁸ Additionally, we support presentation of an expense ratio in the prospectus fee table that would include only ongoing fund expenses. We believe that exclusion of performance expenses from the proposed "Ongoing Annual Fees" calculation would provide investors with a more consistent and appropriate point of comparison between funds. The amount of performance expenses, such as interest expense or dividends paid on short sales, that a fund incurs can vary materially from one year to the next. Material performance expenses could be qualitatively described in a footnote to the prospectus fee table.

⁹ Fee, expense, and performance calculations, however, are categories for which detailed instructions from the Commission help ensure that the presentation of such calculations is as uniform as possible between various funds.

¹⁰ This enumerated list includes a fund's: (1) name; (2) investment objectives or goals; (3) material increases in ongoing annual fees, transaction fees, or maximum account fee; (4) principal investment strategies; (5) principal risks of investing in the fund; (6) investment adviser(s); and (7) portfolio manager(s). *See* Proposal at 615.

¹¹ We agree with the suggestion by the Investment Company Institute recommending that funds include descriptions of changes for which it has filed an amendment to its registration statement pursuant to Rule 485(a). *See*, Letter from Investment Company Institute to Vanessa A. Countryman, Secretary, US Securities and Exchange Commission, dated December 21, 2020.

¹² *See* Proposal at 478.

We recommend that the Commission adjust the proposed 10% of “assets at risk”¹³ threshold in determining whether a risk is principal to address the complexity of risk disclosure more appropriately. As drafted, the 10% “assets at risk” criteria may create a false sense of precision in investors’ understanding of risk disclosure.¹⁴ We recommend that the 10% requirement be replaced with a less prescriptive principles-based guidance that encourages funds to apply a more fulsome approach to analysis of principal risks—one that takes into consideration various relevant factors, such as severity of the risk, probability of the risk occurring, and mitigating factors—and conveys only risks that are reasonably likely to adversely affect a fund in a clear, concise, and understandable manner.¹⁵

We also recommend that the Commission continue to encourage concise disclosure in plain English. Overemphasis on tailoring risk disclosure to each fund may lead to overly technical and complex disclosure that reduces investor engagement. By contrast, concise standard risk disclosure in plain English used across multiple funds—where such disclosure appropriately describes risks tied to how the particular fund operates—would increase the ease of comparison between funds for investors.¹⁶

C. Reconsider Changes to Liquidity Risk Management Disclosure Requirements

We urge the Commission to reconsider the proposal to replace current liquidity risk management program disclosure with a brief summary of: 1) key factors or market events that materially affected the fund’s liquidity risk during the reporting period; 2) key features of the fund’s liquidity risk management program; and 3) effectiveness of the fund’s liquidity risk management program over the past year, tailored to each fund where appropriate.¹⁷

We believe the current disclosure framework appropriately discusses funds’ liquidity risk management program and liquidity risk. In particular, for funds meeting the definition of an “In-Kind ETF” or a “Primarily Highly Liquid Fund” under Rule 22e-4 (Highly Liquid Funds), we do not believe that tailored liquidity risk management disclosure furthers the Commission’s goal of highlighting key information and risks for investors. We believe that, in practice, the proposed changes would result in overly complicated and lengthy disclosure. Therefore, we recommend that the Commission allow at least Highly Liquid Funds to continue to rely on the current

¹³ See Proposal at 314-315.

¹⁴ A false impression of precision could lead to unworkable expectations and undue litigation risk for funds. We would not, for example, expect funds to file amendments under the proposed framework each time a dynamic market event caused the fund’s level of assets at risk to rise just above or fall just below 10%. Moreover, market conditions’ impact on a fund are discussed in the Management’s Discussion of Fund Performance included in shareholder reports.

¹⁵ See Accounting Disclosure Release, ADI 2019-08, Improving Principal Risks Disclosure, *available at* <https://www.sec.gov/investment/accounting-and-disclosure-information/principal-risks/adi-2019-08-improving-principal-risks-disclosure>. The Staff has, in the past, acknowledged that “funds may reasonably consider different factors in determining which risks are most important or weigh factors.” *See id.*

¹⁶ See ADI 2019-08, Improving Principal Risks Disclosure.

¹⁷ See Proposal at 616.

liquidity risk management program disclosure framework. Additionally, we believe this information would be most appropriately disclosed on a Highly Liquid Fund's Form N-CSR.

III. Fund Complexes Should Retain the Ability to Include Multiple Funds in Shareholder Reports

We urge the Commission to continue to provide fund complexes the option to include multiple funds in a single shareholder report. While some series of a registrant may be marketed separately, other series may be presented as part of a suite of investment options.¹⁸ In such instances, shareholder reports that present the full suite of investment options in one report can help investors better understand the fund in which they are invested. Moreover, the shortened length of the proposed shareholder reports would make any combined shareholder report easier to navigate.

IV. Operational and Cost Considerations

We strongly urge the Commission to replace the requirement to provide notices of material fund changes to investors within three business days with a requirement that notices be provided as soon as reasonably practicable.¹⁹ Without this modification, funds with large shareholder bases, including many Vanguard funds, may not be able to operationally meet the requirements necessary to rely on Rule 498B. This would result in a lower adoption rate of Rule 498B and investors continuing to receive multiple disclosure documents that include very similar information every year. It would also result in increased fund expenses for shareholders to bear. Such results would run contrary to the intent of the Proposal.

We believe that certain of the proposed changes may result in outsized costs to funds when compared against the benefit the Commission is seeking to achieve. Notably, the Proposal seeks to narrow the definition of a "broad-based index" to one that reflects "the overall applicable domestic or international equity or debt markets, as appropriate."²⁰ The proposed narrowing of this definition could create a market dynamic in which the entire mutual fund industry would have licensing agreements with just a handful of index providers. While we support the aim of providing shareholders with a market comparison, such general market performance is readily available online. We believe that the potential licensing cost increases for the mutual fund industry, which would be borne by shareholders, outweighs the benefit to shareholders in requiring funds to utilize a narrow set of broad-based indexes in their disclosure documents.

Finally, in recognition of the comprehensive changes to the disclosure framework that the Proposal presents, we ask that the Commission allow for at least 24 months to comply with any final rule.

* * *

¹⁸ For example, target date funds and lifestyle funds.

¹⁹ See Proposal at 466-467.

²⁰ See Proposal at 610.

Vanguard appreciates the opportunity to comment on the Proposal. We welcome the opportunity to continue partnering with the Commission on these important issues. If you have any questions or would like to discuss our views further, please contact Tara R. Buckley (tara_r_buckley@vanguard.com) or Natalie Bej (natalie_bej@vanguard.com).

Sincerely,

/s/ Anne E. Robinson

Anne E. Robinson
General Counsel and Managing Director
The Vanguard Group, Inc.

cc: The Honorable Jay Clayton, Chairman
The Honorable Hester M. Peirce
The Honorable Elad L. Roisman
The Honorable Allison Herren Lee
The Honorable Caroline A. Crenshaw
Dalia Blass, Director, Division of Investment Management