MUTUAL FUND DIRECTORS FORUM
The FORUM *for* FUND INDEPENDENT DIRECTORS

May 18, 2018

Mr. Brent J. Fields
Secretary
United States Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

Re: Investment Company Liquidity Disclosure (File No. S7-04-18)

Dear Mr. Fields:

The Mutual Fund Directors Forum ("the Forum")[1] welcomes the opportunity to comment on the Commission's recent rule proposals regarding Investment Company Liquidity Disclosure.[2]

The Forum is an independent, non-profit organization for investment company independent directors and is dedicated to improving mutual fund governance by promoting the development of concerned and well-informed independent directors. Through education and other services, the Forum provides its members with opportunities to share ideas, experiences and information concerning critical issues facing investment company independent directors and also serves as an independent vehicle through which Forum members can express their views on matters of concern.

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In submitting our comments, we wish to reiterate our view that liquidity risk management is an important issue for all funds and that fund boards have an important role to play in overseeing the manner in which this risk is managed. That said, we continue to have concerns about the Commission's approach to liquidity risk management – in particular, we echo the concerns of our membership that the recently adopted requirement that funds classify every portfolio security into a specific "liquidity bucket" will impose significant costs on funds and their shareholders without producing commensurate benefits or otherwise improving the manner in which the industry manages liquidity risk. While not the subject of this rulemaking, we encourage the Commission to also reopen this aspect of the rule and consider focusing on providing funds and directors with a principles-based approach to managing and overseeing liquidity risk.

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1 The Forum's current membership includes over 976 independent directors, representing 126 mutual fund groups. Each member group selects a representative to serve on the Forum's Steering Committee. This comment letter has been reviewed by the Steering Committee and approved by the Forum's Board of Directors, although it does not necessarily represent the views of all members in every respect.

2 Investment Company Liquidity Disclosure, Release No. IC-33046, 83 Fed. Reg. 11,905 (Mar. 19, 2018) ("Proposing Release").

That said, we strongly support the Commission's proposal to revise the rule's approach to disclosure. Specifically, we concur with the Commission's intuition that providing fund shareholders with highly detailed disclosure information on how the fund has bucketed its portfolio securities on an aggregate basis is unlikely to be meaningful to investors, and may, in certain circumstances, be unintentionally misleading.[3] Rather, as we discuss in more detail below, we believe that fund shareholders should consider liquidity risk in the context of all risks posed by a particular fund.

In determining whether to invest in a fund, investors consider, among other things, the various risks that could prevent the fund from achieving its objectives. Hence, it is critical that investors be informed about those risks in the fund's prospectus and in its periodic disclosure. Once provided with this disclosure, investors ought to consider holistically all the risks posed by a fund in the context of the fund's objectives rather than considering any specific risk in isolation.

As adopted, the liquidity risk management rule undermines this approach to risk. Specifically, it requires funds to disclose information about how a fund has bucketed its portfolio securities on a discrete disclosure form. This disclosure does not provide investors with an analysis of the liquidity risks posed by the fund, but rather amounts to little more than a series of data points regarding the fund manager's seemingly subjective understanding, on an aggregate basis, of the relative liquidity of the securities that constitute the fund's portfolio. Moreover, given the rule's disclosure timing provisions, this information will be out of date and potentially stale. Finally, given that the information is presented in a separate form, whatever information it does convey about liquidity risk is not presented in the context of the other risks and benefits of investing in the fund. Presented in this manner, this data about a fund's liquidity position is unlikely to provide useful information to an investor trying to decide whether to invest in or remain invested in a fund.

The proposed approach, in contrast, will be much more effective. As described in the Proposing Release, funds would be required to provide a description in the annual Management Discussion of Fund Performance of "the operation and effectiveness of the Fund's liquidity risk management program during the most recently completed fiscal year."[4] Notably, the Commission anticipates that this disclosure would "provide investors with enough detail to appreciate the manner in which a fund manages its liquidity risk."[5] As we construe this proposal, the newly mandated disclosure will provide investors, in plain English, with a concise narrative that is appropriate to both the liquidity risks posed by a particular fund's investment strategy and the

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3 We note, however, that although this amendment would eliminate the requirement that funds publicly disclose information on the bucketing of individual portfolio securities, the rule continues to require submission of this information to the Commission. We share the concerns of other commentators regarding the importance of maintaining the security and integrity of this information and encourage the Commission to take all necessary steps to protect it, including delaying, if necessary, the effective date of the rule to address data security issues. In addition, we urge the Commission to proceed with caution when analyzing differences in results between funds, as different assumptions, ambiguity inherent in the rule, and different size of portfolio holdings may lead to markedly different results for similar holdings.

4 Proposing Release, *supra* note 2, at 11,910.

5 *Id.*

manner in which that particular fund manages its liquidity risk. Pursuant to the rule, investors will find this narrative in the context of a discussion of the fund's investment objectives and performance and along with descriptions of other risks posed by the fund.

This revised disclosure provides funds with the leeway necessary to explain to their investors and potential investors contextually the liquidity risks faced by the fund and the manner in which the fund manager mitigates those risks. It also appropriately eliminates the need for funds to disclose an aggregate summation of the series of determinations about how they bucket securities that are of little apparent use to their investors. Combined with existing requirements that a fund disclose its principal risks in its prospectus,[6] we agree with the Commission that this is the most effective manner to provide information on a fund's management of liquidity risk to its shareholders, in a format that will allow those investors to assess the importance of the information as it relates to their broader investment and savings goals. In contrast to the current disclosure requirements, this revised requirement will improve the overall quality of fund disclosure and thus benefit fund investors.

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For the reasons outlined above, we support the Commission's revised approach to liquidity risk disclosure. We would welcome the opportunity to further discuss our views with you. Please feel free to contact Susan Wyderko, the Forum's President, at [redacted] or David Smith, the Forum's General Counsel, at [redacted] if you should like to do so.

Sincerely,

David B. Smith, Jr.
Executive Vice President and General Counsel

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6 As the Commission notes in the Proposing Release, a fund is already required to disclose "liquidity risk if applicable" as an element of its prospectus disclosure of the principal risks of investing in the fund. *Id.; see also* Items 4(b) and 9(c) of Form N-1A.