WELLINGTON MANAGEMENT COMPANY LLP
280 Congress Street, Boston, MA 02210 USA

T +1.617.951.5000
www.wellington.com

WELLINGTON
MANAGEMENT

13 January 2016
Mr. Brent J. Fields
Secretary
United States Securities and Exchange Commission
100 F Street, NE
Washington, DC 02059-1090

VIA E-MAIL: rule-comments@sec.gov

Re: Open-End Fund Liquidity Risk Management Programs; Swing Pricing
File No. S7-16-15
Re-Opening of Comment Period for Investment Company Reporting Modernization
File No. S7-08-15

Dear Mr. Fields:

Wellington Management Company LLP ("**Wellington Management**") appreciates the opportunity to respond to the request for comments from the Securities and Exchange Commission (the "**Commission**" or "**SEC**") on the proposed rules regarding Open-End Fund Liquidity Risk Management Programs (the "**Proposal**"). Wellington Management is a private partnership registered as an investment adviser. As of December 31, 2015, we managed over $925 billion in assets across a wide variety of equity, fixed income and asset allocation strategies. Tracing our roots back to 1928 with the establishment of the first balanced mutual fund, the Wellington Fund, Wellington Management has managed mutual funds for 88 years. While we do not sponsor mutual funds in the United States, we currently manage approximately $450 billion as sub-adviser to 239 mutual funds representing 39 fund family relationships.

We fully support the Commission's efforts to "raise the bar" of liquidity risk management for funds and to provide more information to fund shareholders regarding the liquidity risk of funds. However, as discussed at some length in the Proposal, liquidity evaluation and liquidity risk management is a complex affair, often more art than science, and the structure of liquidity in markets varies over time. Given this complexity and variability, we urge the Commission to adopt a more dynamic approach than the one described in the Proposal (the "**Proposed Program**"). We propose that the Commission instead adopt a rule that requires funds to adopt written liquidity risk management programs, rather than one mandating a particular liquidity risk management approach. In this way, funds would be encouraged to design programs tailored to the particular risks faced by each fund and adapt those programs as markets evolve and as new tools become available.

While we have substantive concerns about the liquidity risk management approach described in the Proposal, our primary concern with the Proposal relates to the proposed public disclosure of the liquidity metrics generated under the Proposed Program. Public disclosure of liquidity classifications or other estimates could be confusing and misleading to investors. We strongly support providing the Commission and fund investors with additional information to help them better understand the liquidity risk of funds. Unfortunately, a sufficiently objective market convention to measure liquidity has not yet been developed. Disclosures that suggest that one does would be misleading. Therefore, we encourage the Commission to require funds to provide a qualitative discussion of liquidity risks in fund offering documents. We also suggest that the Commission use data gathered under the proposed Form N-PORT[1] and through industry outreach to provide guidance on additional liquidity data that would be useful to the investing public. We also support sharing certain more detailed liquidity risk information with the Commission to support its oversight efforts, provided this information is not publicly disseminated.

LIQUIDITY RISK MANAGEMENT IS TOO COMPLEX FOR A SINGLE SOLUTION

The Complexity of Liquidity Risk Management Requires a Variety of Approaches

Funds offer their shareholders access to professional investment management services with daily liquidity. This daily liquidity necessarily comes at the cost of some risk of dilution from the activities of other shareholders. While this trade-off is a fundamental part of pooled investing, we firmly believe that funds and their managers have a fiduciary duty to manage liquidity risks. Indeed, the asset management industry has already developed many different approaches to managing fund liquidity risk. No single approach has distinguished itself as a better or universally effective approach to liquidity risk management.[2] These distinct approaches may differ by firm and some firms may employ different approaches to manage different funds. For example, we have developed our own liquidity measurement tools which include a portfolio-level liquidity assessment engine and a security-level liquidity scoring system. We employ these tools where they are helpful in managing liquidity risk, but not necessarily in the same manner or in the same frequency for all client accounts.

Our approach is one of many. Some managers may assess liquidity at the portfolio level rather than at each position. Firms may employ entirely different tools to assess equity liquidity than they use for fixed income liquidity. Some use simulations, while others rely on more qualitative inputs. Firms can reasonably differ in their expectations of the impact of various market events and, as a result, evaluate the same factors differently or evaluate different factors altogether. Some firms could evaluate liquidity not in terms of how much of the fund's portfolio could be liquidated in certain time frames, but rather, based on how much impact a forced liquidation would have on the fund's net asset value ("**NAV**") at various redemption levels. We believe any and all of the above approaches represent valid methods for evaluating fund liquidity risk, and that all are more or less effective for different funds at different times.

Given the complexity and consistently changing nature of liquidity we do not believe it is possible to develop a single program that could be universally applied to all funds. Liquidity evaluation is necessarily predictive and thus imperfect. Moreover, markets for different securities can be vastly different. Principles that work well for evaluating large cap equities do not necessarily apply to high yield bonds. Different funds may warrant the use of entirely different tools to effectively manage the fund's liquidity risk. A fund offered exclusively through a variable insurance wrapper will have different liquidity risks than a high yield bond fund with a small number of large institutional shareholders.

Indeed, liquidity, itself, is subject to constant change as are the tools that attempt to measure it. As recently as ten years ago, liquidity was driven by the willingness of banks and brokers to purchase assets. Today, asset managers and institutional investors are major drivers of liquidity. During that same ten year period, we have seen the development of new technology, tools and data useful in monitoring liquidity risk. In recent years, we have observed our clients, peer firms and data service providers investing significantly in liquidity evaluation, rapidly developing new and innovative tools to estimate portfolio and security liquidity, including tools that apply artificial intelligence to discover relationships between securities that have henceforth been undetected.

---

1 Proposed Rule: Investment Company Reporting Modernization, SEC Rel. No. IC-31610.

2 The Association of the Luxembourg Fund Industry reached to a similar conclusion, noting "there seems to be no empirically validated, robust and widely accepted models in the market yet, even though some proposed models and methodologies claim to be empirically validated, robust and/or widely accepted." UCITS Liquidity Risk Management Guidelines, page 10.

The Proposed Program illustrates our concerns regarding the application of a single program to all funds. It would require all funds to perform a position-level analysis and evaluate factors determined by the Commission to be relevant in assessing their positions, whether or not these metrics are most appropriate for evaluating the fund's liquidity risk. While this position-level analysis may be appropriate for equity funds, we believe it falls short when applied funds holding certain types of fixed income instruments, e.g., bank loans, municipal securities and agency mortgage backed securities.[3] Positions in fixed income instruments, especially instruments for which there is limited historical liquidity data, cannot always be placed into categories based on their ability to be converted to cash with any degree of reliability. This categorization suggests a precision in analysis that simply cannot exist with liquidity evaluations of these instruments.

Even if this information could be precisely generated, we believe it could systemically overstate the liquidity of the fund as a whole. The categorizations required under the Proposed Program would require funds to evaluate positions independently, and therefore do not account for portfolio-interdependence, i.e., the tendency of selling one position to impact available liquidity for selling other positions. In certain asset classes, especially in fixed income, the sale of one asset can reduce the available liquidity for a similar asset.

We also believe that requiring any single liquidity risk management approach across all funds would result in significant unintended adverse consequences. Not all funds have unlimited resources to devote to this single risk. A uniform program requirement could cause some funds to build programs that meet minimum regulatory requirements instead of developing tailored programs that would be more useful in managing the liquidity risk of those particular funds. Fund advisers could shift resources from programs that have already proven effective to the required regulatory program. Liquidity risk management would be reduced to a check-the-box discipline.

In addition, we are concerned that any one-size-fits all solution would stifle innovation in liquidity risk management. Our own liquidity risk management tools have evolved considerably over the past ten years. These tools will continue to evolve as markets change; we suspect that we will be able to bring entirely new tools to bear in the next ten years. While a universal program requirement would set a minimum bar, it would fail to provide funds with the incentive or the flexibility to continue evolving liquidity risk programs as markets change – unless the Commission revises its requirements on a regular basis.

Benefits of a Flexible Program Requirement

The Commission has addressed similar areas of complexity and variation in practice without requiring a specific, universal approach. In adopting Rule 38a-1, the Commission noted that "funds and advisers are too varied in their operations for the rules to impose a single set of universally applicable required elements [of a compliance program]. Each adviser should adopt policies and procedures that take into consideration the nature of that firm's operations."[4] We believe that this principle is equally applicable in the context of liquidity risk management.

A flexible program liquidity risk management program requirement is most likely to accomplish the Commission's goal of ensuring that all funds have effective liquidity risk management programs, in large part because it would preserve the ability for funds to tailor their programs to their own activities. Funds would have an obligation to design programs that fit their specific needs. The data produced under these programs would be valuable to fund boards evaluating

---

3 Under the Proposed Program, funds would be required to consider the typical expected settlement period when determining the "days to cash." Agency mortgage backed securities ("MBS") can have settlement cycles, based on customary market practice, anywhere from 2-60 days from trade date. However, these securities are some of the most liquid securities in fixed income markets. Additionally, in typical agency MBS TBA ("to be announced") transactions, the fund continues to hold the cash committed under the TBA until settlement date, significantly mitigating liquidity risks of these instruments.

4 Final Rule: Compliance Programs of Investment Companies and Investment Advisers, SEC Rel. No. IC-26299.

liquidity risk and to SEC examiners assessing the fund manager's views on this risk. Funds would have room to adapt their programs to changing market conditions and available tools. A flexible program requirement would also avoid misdirecting resources into developing liquidity risk reports that are not actually used by the fund to manage liquidity risk.

The flexible program requirement also supports the Commission's goal of promoting a minimum baseline of liquidity risk management. The Commission could promote minimum standards by adopting required program elements, e.g., that the programs be in writing and subject to annual board review, recordkeeping and back-testing. In addition, the Commission and its staff could publish guidance to funds that sets forth the Commission's expectations as those expectations evolve based on information gained from examinations, inspections, and the new data funds will be providing about their holdings on N-PORT. Commission examination staff could require any funds who are not meeting the standards set forth in the Commission's guidance to explain any deviations from its guidance. In this way, we believe that a flexible requirement would both set a minimum baseline of liquidity risk management and provide room for liquidity risk management programs to evolve over time. Indeed, Commission and SEC staff guidance in this area would encourage funds to meet emerging best practices and adopt new liquidity evaluation tools as they became available.

In sum, a flexible liquidity risk management rule promotes the adoption of effective liquidity risk management programs while avoiding the significant complications of attempting to design, by regulation, a liquidity risk management program applicable to all types of funds – a task that we believe will ultimately prove futile. We believe the Commission could better accomplish its goals of improving fund liquidity risk management if it views the liquidity risk management rule not as a single solution to fund liquidity risk, but rather as the first step in a longer process of fostering effective liquidity risk management over time.

DISCLOSURE OF LIQUIDITY INFORMATION

While we do not believe the Proposed Program (or any single program requirement) would best advance the goals of the Commission outlined in the Proposal, our most significant concern with Proposal is the proposed public dissemination of liquidity metrics, specifically the liquidity classifications required under the Proposed Program. We support the Commission's goal to improve the ability of investors and the Commission staff to better understand a fund's liquidity risk. However, we do not believe the classification information represents a valuable metric for comparison across funds. Moreover, we believe that these classifications would be confusing and/or misleading to fund shareholders. As a result, we strongly oppose the proposed amendments to N-PORT that would require disclosure of a fund's liquidity classifications. We believe the Commission could accomplish its goal of informing investors and the Commission staff of fund liquidity risks through other measures that do not carry the same risk of confusion to investors.

Liquidity Classifications would not Provide Valuable Information to Investors

As a threshold matter, we are unconvinced that the position liquidity classification would provide consistently valuable information for fund liquidity risk management for all types of funds. The particular liquidity classifications required under the Proposed Program imply a precision and objectivity that does not exist in liquidity risk management. In the Proposal, the Commission recognized the complexity of liquidity evaluations and that even its liquidity classifications inherently involve judgment, especially for fixed income funds. Different funds will make different assumptions with respect to the countless variables involved in liquidity evaluation. The classification regime included in the Proposal nonetheless suggests that, despite the complexity of the unspoken underlying judgments, it is possible to objectively determine the specific number of days it would take to convert a position to cash. Investors evaluating these categorizations would reasonably assume that these categorizations were factual, not merely informed estimates. In our experience, these estimations have a significant margin for error, often larger than the individual categories prescribed under the Proposed Program.

At the same time, the data will have limited relevance to investors because it will be stale by the time it is disclosed. Market conditions, fund positioning, other investment opportunities, and countless other variables could change a position's classification almost immediately. The Commission implicitly recognizes the ephemeral nature of these determinations when it suggests that funds may want to review liquidity classifications frequently. It seems inherently contradictory to suggest that funds should review data as frequently as hourly, but at the same time suggest that the same data would be valuable to the investing public when published on a quarterly basis 60 days after the reporting period.

Liquidity Classifications Could be Confusing and/or Misleading

We are also concerned that this classification system could be confusing and/or misleading to shareholders and other fund investors. As one example, the classification system would make larger funds appear less liquid than smaller ones, as a greater proportion of the larger fund's assets would necessarily be categorized in the longer-dated classifications. This could lead investors to favor smaller funds, which, ironically, for day to day investors actually pose greater liquidity risks. The proposed classification system would tend to over-state position liquidity because it fails to account for the impact of other trading activity of other clients managed by the same investment adviser. In addition, the proposed classifications do not account for "portfolio interdependence", a phenomenon especially present in fixed income funds where the sale of one position could have an impact on the liquidity of a second, similar position.

We also disagree that third-party data analyzers could use this classification information to produce useful metrics for investors. The subjective nature or this data renders comparable metrics impossible, at least with any degree of accuracy. Instead, we anticipate that these third-party data analyzers would digest liquidity classification information to a single metric, a fund liquidity score that would be widely published, similar to (and likely along with) an fund's "star" rating. We think this would serve to misinform investors. Liquidity risk evaluation is a complex and nuanced process that should not be communicated to potential investors as a single "liquidity star rating."

Alternative Disclosure Requirements

Most, if not all of these concerns, can be addressed by eliminating the requirement for funds to affirmatively disclose their classifications (this information would still be available to Commission staff in examinations/inspections) or by requiring that any disclosure be made to the Commission confidentially. While we do not believe that classification information should be made public, we agree with the Commission that shareholders should have additional information regarding fund liquidity. We propose that the Commission require funds to include a qualitative discussion of their liquidity risk profile. In addition, as liquidity risk management programs evolve, we believe the Commission could provide guidance on objective data that could be disclosed to shareholder that would describe a fund's ability to satisfy redemption requests and be comparable across funds. This is the information we believe interests shareholders and investors, rather than estimates of how long it would have taken to receive cash for each of the fund's positions if sold individually and entirely – several months ago.

We also support the Commission's efforts in gathering information on fund investments generally, but we believe the information produced under the Proposed Program would be of limited value to the Commission. This data would be based on subjective judgment of the funds and their advisers, so the data will not be comparable among funds nor aggregable. As such, we do not believe the information produced under the Proposed Program would be helpful to the Commission in effecting its mission.

The Commission will soon have access to an unprecedented amount of information regarding fund investments. With the adoption of the Investment Company Reporting Modernization proposed rule, the Commission will be able to garner a great deal of liquidity information from the disclosure proposed to be provided under N-PORT. Based on that data, the Commission will be able to make comparisons of position sizes against a great deal of publicly available data (e.g., trading volume, issuer float, etc.). Should the Commission need assistance in those calculations, N-PORT could be amended accordingly (e.g., for equity securities, funds could provide the size of each position as a percentage of average daily trading volume and/or total issue size as an additional field in N-PORT).

We urge the Commission to take a measured approach here as well, adopting a qualitative disclosure requirement. At a later date, once all funds have established liquidity risk management programs and the Commission has had the opportunity to analyze the data it will receive regarding fund portfolio holdings, it should consider requiring funds to provide the Commission data on fund liquidity assessments on a confidential basis.

CROSS TRADING

In the Proposal, the Commission requested comments on cross-trading, specifically, whether the Commission's guidance with respect to Rule 17a-7 provided sufficient protections to investors. Rule 17a-7 permits funds to engage in cross trades at the "current market price" of the traded securities. For securities not traded on an exchange, this "current market price" is based on the "average of the highest current independent bid and lowest current independent offer determined on the basis of reasonable inquiry."[5] Current SEC staff guidance permits funds investing in municipal securities to utilize market data service providers to determine "current market price," subject to certain conditions.[6]

We believe that this guidance should be updated to clearly permit funds investing in other types of fixed income securities to also utilize data service providers for pricing cross trades. As the result of recent banking regulations and changes to market structure, dealers in bonds are less willing to buy and sell bonds than they have been in the past and are therefore also less forthcoming with the bids and offers that would support the pricing determination required under Rule 17a-7. Allowing funds to use data service providers to establish "current market price would expand the ability for funds to engage in cross trades and would provide another avenue for funds to raise liquidity. This use of data service providers to price cross trade transactions should not pose any threat of overreaching or abuse where the data service provider used for pricing cross trades is the same data service provider used by the fund for determining the value of the securities for calculating the fund's NAV.

---

5 Rule 17a-7(b)(4).

6 Federated Municipal Funds, SEC No Action Letter (pub. avail Nov. 20, 2006).

*   *   *

We appreciate the opportunity to comment on the Proposal. If you have any questions about our comments or would like any additional information, please contact me or Lance Dial at the number above.

Very truly yours,

Cynthia M. Clarke
Cynthia M. Clarke
General Counsel
Wellington Management Company LLP

CC:
The Honorable Mary Jo White, Chair
The Honorable Kara M. Stein, Commissioner
The Honorable Michael S. Piwowar, Commissioner
David Grim, Director, Division of Investment Management