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January 13, 2016

Mr. Brent Fields
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

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

Dear Mr. Fields:

J.P. Morgan Asset Management ("JPMAM")[1] is pleased to respond to the Securities and Exchange Commission's (the "SEC" or the "Commission") request for comment on its proposal on liquidity risk management programs for open-end funds (the "proposal"). JPMAM offers 155 mutual funds and ETFs in the US (excluding money market funds), with a total of approximately $268 billion in assets under management at the end of 2015.

JPMAM supports the SEC's goals of promoting effective liquidity risk management throughout the open-end fund industry, reducing the risk that funds will be unable to meet redemption obligations, and mitigating dilution of the interests of fund shareholders. We believe the SEC, as the primary regulator of the asset management industry, is well placed to promulgate regulations regarding liquidity risk management, and to supervise funds and monitor potential liquidity risks on an ongoing basis.

More specifically, JPMAM supports the SEC's general approach to liquidity risk management for funds. We believe enhanced liquidity monitoring and reporting obligations, along with an enhanced oversight and governance framework, will improve funds' ability to manage their liquidity risks. At the same time, we appreciate the Commission's recognition that, for a range of reasons, different funds have different liquidity profiles, and therefore a one-size-fits-all approach to liquidity management (such as by requiring specified cash buffers or other liquidity allocations) would not be helpful.

[1] J.P. Morgan Asset Management is a marketing name for the investment management subsidiaries of JPMorgan.

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J.P. Morgan Investment Management Inc.

We write to provide comments on certain critical elements of the proposal. Our comments underscore our view that markets and liquidity are dynamic. We support the SEC's proposed approach of assessing a the liquidity of a fund's portfolio securities on a continuum from most to least liquid, rather than the current bilateral construct under SEC guidance, in which assets are considered to be liquid if they are not in the 15% illiquid bucket. We believe that, even when market conditions change dramatically, *relative* assessments of liquidity should typically hold, *i.e.,* assets classified as more liquid are likely to remain more liquid than those classified as less liquid. At the same time, during highly stressed markets, even the most liquid assets could experience more price volatility and lower market depth than during ordinary markets. For these reasons, we have concerns about how the proposal articulates its liquidity categories, as well as the concept of the "three-day liquid asset minimum." We also offer our views on the proposal's reporting and disclosure requirements, and swing pricing.

Our comments can be summarized as follows:

- Classification of Liquidity of Portfolio Positions: JPMAM supports a requirement that funds classify their portfolio holdings across a spectrum of liquidity. However, we have several concerns with the proposed approach, including the granularity of and precision implied by the proposed six buckets based on the estimated days to liquidate a position, as well as the requirement that a sale must not materially impact the price of the asset. We offer an alternative approach that we believe would meet the Commission's objectives of enhancing a fund's ability to monitor and manage its liquidity and providing sufficiently granular data for the Commission to monitor liquidity risk in funds and identify outliers.

- Management of Liquidity Risk – Three-Day Liquid Asset Minimum: JPMAM supports improving funds' consideration of, and placing a governance structure around, the maintenance of highly liquid assets. We are concerned, however, that the proposed three-day liquid asset minimum, which requires board approval, is not sufficiently dynamic to respond to changing market conditions, and does not offer sufficient flexibility to manage funds efficiently. We also have concerns about the proposed liquidity classifications based on "days to liquidate." We recommend instead that the board oversee a management committee that supervises a highly liquid asset threshold.

- Reporting and Disclosure Requirements: While we support monthly reporting to the SEC of the information described in the rule (subject to our comments), as well as additional disclosure to investors on Form N-1A, we question the value of quarterly disclosure of liquidity classifications and the three-day liquid asset minimum to the public. We are concerned that the classifications could be used to provide outdated metrics about a fund's portfolio. Disclosure of the liquid asset minimum or threshold could also have unintended consequences.

- Swing Pricing: We generally support the proposal to permit funds to use swing pricing. We recommend that the Commission permit, but not require, the consideration of market impact in setting a swing factor, and we suggest more flexibility in the factors for establishing a swing threshold. We also describe some operational challenges that we hope the industry will resolve should the Commission permit swing pricing.

Classification of Liquidity of Portfolio Positions

JPMAM supports the concept of requiring funds to analyze the liquidity of their portfolios, and to monitor these classifications on an ongoing basis. We believe liquidity exists on a spectrum from highly liquid to illiquid. Analysis of how a portfolio's assets are spread across this range is an important input into the assessment, monitoring, and management of a fund's liquidity risks.

While we support the concept of a position-level assessment of liquidity, we have several comments and concerns with the proposed approach to this assessment – specifically, the proposed classification of funds' positions into six categories based on the time period in which the position "would be convertible to cash at a price that does not materially affect the value of that asset immediately prior to sale." Our concerns are set out below, after which we offer an alternative approach.

As a preliminary matter, the SEC's proposed factors to be considered in classifying the liquidity of positions are generally consistent with our view of relevant inputs to such an analysis.[2] However, because we agree that the enumerated factors may not apply to all funds or instruments, and are also not an exhaustive list, we recommend that these factors be provided as guidance in an adopting release, rather than enumerated in the rule text.

With respect to the proposed liquidity classifications, we note that outside of US equities and a limited range of government bonds, an assessment of days to convert a position to cash can be highly subjective and imprecise, even without the added stipulation that the transaction must not materially affect the value of the asset. Importantly, such an estimate is likely to be most inaccurate when it is most scrutinized – that is, during unpredictable market events or volatility. Even in normal market conditions, these assessments could change from week to week or even daily. We are thus concerned that the proposed "days to liquidate" designations imply a false sense of

[2] These factors are: existence of an active market for the asset, including whether the asset is listed on an exchange, as well as the number, diversity, and quality of market participants; frequency of trades or quotes for the asset and average daily trading volume of the asset (regardless of whether the asset is a security traded on an exchange); volatility of trading prices for the asset; bid-ask spreads for the asset; whether the asset has a relatively standardized and simple structure; for fixed income securities, maturity and date of issue; restrictions on trading of the asset and limitations on transfer of the asset; the size of the fund's position in the asset relative to the asset's average daily trading volume and, as applicable, the number of units of the asset outstanding; and relationship of the asset to another portfolio asset.

precision. Our concern is compounded by the designation of six categories – this level of granularity further implies a level of precision which is unrealistic in most asset classes.

The proposed liquidity assessment is further complicated by the requirement that conversion to cash must not materially affect the value of the asset. We recognize the concern underlying this requirement, namely that if funds sell assets at "fire sale" prices there can be negative price pressure on those assets as well as correlated assets, which could transmit stress to other funds or portions of the market.[3] In theory, almost any security can be sold quickly with a high enough discount; we therefore acknowledge the Commission's desire to impose some boundary on the price at which an asset can be converted to cash in order to qualify as liquid.

However, the requirement that a conversion must not affect the value (or not "materially") discounts two very important facts. First, buying or selling virtually any position size by definition affects pricing, with the possible exception of relatively small blocks of actively traded securities. Moreover, even for the most liquid instruments, in dynamic markets prices change constantly. From a practical perspective, it would be impossible to determine the potential effect of an individual trade on an asset's price in order to comply with such a requirement.

As important, while mutual funds promise daily redemptions, there has never been an expectation that such redemptions must take place without impacting market prices. Investors understand that sales of fund portfolio assets in a declining market could result in the fund receiving less than the asset's carrying value. Such investment risk is fundamental to the success of the capital markets and to mutual funds themselves. Any suggestion that mutual funds offer some level of price certainty should be treated with extreme caution.

To address these concerns while remaining consistent with the proposal's approach of classifying liquidity on a continuum, we recommend that funds be required to conduct position-level assessments and classify assets into five buckets with descriptors that connote *relative* liquidity, while removing the "days to liquidate" indicator. These buckets are described below. To provide additional color, we have included examples of security types that we would generally consider for each bucket if we were to conduct such an analysis today. We would not recommend that these examples be codified in the final rule, however, because as we have explained, markets are dynamic and conditions change frequently. As a result of the required ongoing monitoring, the illustrative security types we provide could require different classification in response to changing market conditions.

[3] *See, e.g.,* Open-End Fund Liquidity Risk Management Programs; Swing Pricing; re-Opening of Comment Period for Investment Company Reporting Modernization Release, Release Nos. 33-9922, IC-31835 (Sept. 22, 205), 90 Fed. Reg. 62274 (Oct. 15, 2015) ("Proposing Release") at 24.

1) Cash and cash equivalents: "daily liquid assets" as defined in Rule 2a-7, *i.e.,* i) cash, ii) direct obligations of the U.S. Government, or iii) securities that will mature or are subject to a demand feature that is exercisable and payable within one business day;

2) Highly liquid instruments: instruments with daily trading/widely available market quotes even during periods of market stress (*e.g.*, large cap equities, G4 government and agency bonds (US, UK, Germany and Japan), new issue US Agency MBS passthroughs, investment grade corporate bonds that have large amounts outstanding and are constituents of major benchmarks);

3) Moderately liquid instruments: instruments that are considered liquid in ordinary markets, but which may become less liquid in stressed conditions (*e.g.,* most high yield bonds, major emerging market equities, investment grade corporate bonds other than those described above, "Tier 1" EMD sovereign bonds, senior tranche RMBS and CMBS);

4) Less liquid instruments: instruments for which there are few active participants, execution is sporadic and/or in small sizes (*e.g.,* non-rated municipal securities, high yield bonds that are particularly vulnerable to a negative credit event, frontier country EMD sovereign bonds, junior tranches of structured products);[4]

5) Illiquid instruments: instruments that are private or restricted securities (other than 144A or similarly liquid securities), internally fair valued, and/or are highly distressed.

We believe assigning portfolio positions to these five buckets, using the SEC's proposed factors[5] as appropriate along with any other relevant information, is preferable to requiring an estimate of "days to liquidate," for several reasons. First, it addresses the Commission's desire to see liquidity analyzed on a spectrum, and its interest in receiving data it can use to monitor liquidity risk in the industry. Although there may be some differences around the margins in how funds assign specific positions to these buckets, this approach also is likely to produce more comparable results across funds compared to the SEC's proposed buckets, which require an element of guesswork (*e.g.*, to determine whether a position will take 7 or 8 days to liquidate).

In addition, our proposed approach negates the need for the requirement that a potential transaction not materially impact the price. As noted above, using a metric of "days to liquidate" requires the imposition of a backstop against selling quickly for pennies on the dollar (*i.e.,* in theory almost any security can be sold quickly with a high enough discount, which the proposal seeks to avoid). Because our approach looks at the market characteristics of each position, there is no need for such

[4] While there may not be standing bids or offers for some instruments in this category, traders execute the desired transactions by contacting a number of potential counterparties.

[5] *See supra* note 2.

a backstop on price; put starkly, a fund could not put a high yield bond in the "highly liquid" bucket on the theory that it could be converted to cash quickly at a 50 percent discount, because the market characteristics of such a bond do not warrant this classification.

Lastly, because our recommended approach is less subjective than an estimate of "days to liquidity," we believe it is more amenable to inputs from third-party service providers. This is particularly important given that the proposal is based on a position-level liquidity analysis. We expect that over time, funds' approach to liquidity classification will look similar to valuation procedures, whereby we receive a data feed with a variety of quantitative information from third-party service providers, which we review and test (daily and retrospectively), and scrutinize any position that triggers a flag. Without such an automated approach to narrow down the securities that require individual attention, it would be challenging to assess liquidity at a position level on an ongoing basis.[6] To ensure that such an approach retains appropriate rigor and supervision, we support the recommendation in the Proposing Release that funds and advisers should review the data quality, methodologies and metrics provided by third parties, and consider the need for modifications to accurately reflect the liquidity characteristics of a given fund's holdings.[7]

In sum, we believe our proposed approach would, consistent with the Commission's intent, enhance a fund's ability to monitor and manage its liquidity and plan how to meet redemptions, and would provide sufficiently granular data to allow the Commission to monitor liquidity risk in funds and identify outliers.

Management of Liquidity Risk – Three-Day Liquid Asset Minimum

JPMAM supports improving funds' consideration of, and putting a governance structure around, the maintenance of highly liquid assets in their portfolios. While we carefully monitor liquidity in our funds and expect that many of our competitors do the same, we recognize that, with no current regulatory requirements in this area, practices vary widely. Given the global concerns about market liquidity[8] and the growing participation of funds in the securities markets, we believe it is sensible to examine how funds determine the appropriate level of highly liquid assets, and to place more

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[6] We estimate that our US funds hold a combined total of over 30,000 individual CUSIPs.

[7] Proposing Release at 82.

[8] *See, e.g.,* Financial Stability Oversight Council 2015 Annual Report, available at https://www.treasury.gov/initiatives/fsoc/studies-reports/Documents/2015%20FSOC%20Annual%20Report.pdf at 4 ("As this evolution of market structure plays out across a broader collection of asset classes and markets, market participants and regulators should continue to monitor how it affects the provision of liquidity and market functioning, including operational risks."); Statement by Mark Carney, Chairman, Financial Stability Board, to the International Monetary and Financial Committee, April 18, 2015, available at https://www.imf.org/External/spring/2015/imfc/statement/eng/FSB.pdf ("Market participants need to be mindful of risks of diminished market liquidity, asset price discontinuities, and contagion across markets.").

rigorous governance and oversight around such considerations. However, we have several concerns with the proposed approach to requiring a three-day liquid asset minimum.

As a preliminary matter, as discussed above, we have concerns about classifying the liquidity of assets by the number of days in which they can be converted to cash without materially impacting the price. We therefore recommend that the "three-day liquid assets" concept be replaced with "highly liquid assets" or "HLA," consisting of cash and highly liquid instruments, *i.e.,* the first two categories of our proposed liquidity classifications.

Perhaps more importantly, and consistent with our view that markets and liquidity are dynamic, we believe that liquidity management likewise ought to be a dynamic process. Markets and outlooks change daily, and portfolio managers have always taken current events into consideration when managing liquidity. By contrast, the proposed requirement that an HLA minimum, and any changes to it, be approved by the fund board will lead to the minimum being relatively static. JPMAM's fund board holds five scheduled meetings per year; even assuming that an HLA minimum was presented at each meeting, we do not believe that this allows for sufficient flexibility.

There are two possible outcomes from such a static approach, neither of which benefits fund investors. Some funds are likely to take a conservative approach and continually maintain an HLA minimum that is appropriate for high-stress or worst-case market environments, even when not demanded by current or foreseeable market conditions. This could have a negative impact on fund returns, and could have the perverse effect of driving investors toward funds with a less conservative approach, and correspondingly higher returns. Alternatively, some boards may agree to approve a low HLA minimum, based on circumstances at the time of the approval; in such cases the fund would presumably increase its liquid holdings as market conditions changed, but subject to limited board oversight.

We are also concerned that an HLA *minimum* could unnecessarily hamper beneficial fund investments. The proposal is clear that a fund that fell below its three-day liquid asset minimum would not be forced to sell less liquid assets to return to its minimum, but would be prohibited from buying additional less liquid assets. Nonetheless, there may be missed opportunities as a result of an absolute minimum, for example if a fund has an impending inflow (*e.g.,* a new mandate) and would like to begin to invest in advance of the flows, or when the level of HLA has been reduced due to appreciation in securities in an upward trending market and additional buying opportunities are identified in less liquid assets. As noted above, these possibilities could lead fund boards to approve artificially low minimums.

To allow for a more dynamic and flexible approach, while ensuring enhanced governance and oversight of the establishment and maintenance of an appropriate level of HLA, we recommend several changes to the Commission's proposal. First, the board should be permitted to delegate its authority to a liquidity management committee comprised of employees of the fund adviser appointed by the board. Much like the current valuation process, the liquidity management committee could, subject to board-approved policies and procedures, have responsibility for establishing, monitoring and, as necessary, approving changes to the maintenance of HLA, based on the factors proposed by the Commission and other relevant information.[9] The committee could report to the board on a regular basis.

Second, rather than an HLA *minimum,* we recommend an HLA *threshold.* The key distinction here is that a fund would not be prohibited from transacting in less liquid assets when the threshold is breached; however, such a breach would necessitate a timely review by the liquidity management committee and a report to the board.

Finally, because a liquidity management committee would be better positioned than the board to oversee HLA on an ongoing basis, we recommend that the liquidity management committee could be charged with maintaining an HLA threshold that is designed to address *current and reasonably foreseeable near-term market conditions.* This standard should improve results for investors by allowing funds to be more fully invested during ordinary markets, while requiring them to be cognizant of and prepared for changing conditions.

Separately, we request that the Commission clarify its intent regarding the use of HLA to meet redemptions. We agree with the SEC that better oversight and governance around HLA may improve liquidity management and reduce the likelihood that funds would need to dispose of less liquid assets at "fire sale" prices to meet redemptions. However, we do *not* believe that the existence of such assets should create an expectation or requirement that redemptions will be funded from those assets. Indeed, such a requirement could actually *create* an incentive for investors to redeem early, to be assured of getting out before the fund depleted its HLA; even absent such "runs," a requirement to meet redemptions from HLA would by definition increase liquidity risk for remaining shareholders.

We are concerned that, based on the language in the proposal, a portfolio manager's election to sell a less liquid asset (and accept a lower price or "liquidity haircut") on or about the same time that the fund experiences redemptions could be viewed as violating the rule. We request that the Commission clarify that, while the HLA requirement is designed to impose specific requirements on and governance around the liquidity management process, the ultimate determination of how to manage the portfolio and meet individual redemptions remains with the portfolio management team.

[9] The SEC's proposed factors to consider in establishing a three-day liquid asset minimum are: the size, frequency, and volatility of historical purchases and redemptions of fund shares during normal and stressed periods; the fund's redemption policies; the fund's shareholder ownership concentration; the fund's distribution channels; and the degree of certainty associated with the fund's short-term and long-term cash flow projections. As with the factors to be considered for purposes of liquidity classifications, we believe the proposed list of factors is not exhaustive and that the appropriate factors will vary by asset class and fund. We therefore recommend that these factors be provided as guidance in an adopting release, rather than enumerated in the rule text.

Reporting and Disclosure Requirements

JPMAM supports the proposed requirements for increased reporting to the Commission on position-level liquidity classifications and other elements of funds' liquidity risk management programs on Forms N-Port and N-CEN. As the primary regulator of the fund industry in the US, the SEC should have the data it needs to monitor fund holdings and liquidity determinations, examine potential outliers and, if an unexpected market event occurs (*e.g.*, the default of a significant institution), quickly assess the potential impact on mutual funds it supervises.

Indeed, we would support the sharing of such information across other financial regulators, subject to thorough consideration of confidentiality and data security issues. In light of the concerns regarding potential systemic risk in the asset management industry both in the US and abroad,[10] we believe the dialogue can only be improved with better data about fund holdings.

We are also supportive of the proposed additional disclosures to investors on Form N-1A regarding the number of days in which a fund will pay redemption proceeds, and a description of the methods they use, such as in-kind redemptions, and available funding sources, such as lines of credit, to fulfill their redemption obligations. We agree with the SEC that this information will improve shareholder and market participant knowledge regarding fund redemption procedures and liquidity risk management. Similarly, for funds that elect to use swing pricing, the proposed disclosure will be important to enhance public understanding regarding the benefits and risks of swing pricing.[11] We would further support the Commission requiring funds to include a discussion of their liquidity risk management policies and procedures, similar to what is currently required on Form N-1A for policies and procedures regarding proxy voting (items 17 and 27) and valuation procedures (item 23), among others.

On the other hand, we question the value of providing quarterly public disclosure of liquidity classifications. If, as the Proposing Release suggests, third-party data analyzers used this information to produce metrics for investors, which would presumably be updated quarterly in conjunction with each public disclosure, such metrics could be nearly *five months old* when they are replaced (every three months plus a 60-day lag). As such, they may no longer represent the fund's current portfolio composition and liquidity profile. While index funds and others that intentionally manage to their

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[10] *See, e.g.,* Financial Stability Oversight Council, Notice Seeking Comment on Asset Management Products and Activities (Dec. 24, 2014), available at https://www.treasury.gov/initiatives/fsoc/rulemaking/Documents/Notice%20Seeking%20Comment%20on%20Asset%20Management%20Products%20and%20Activities.pdf; Financial Stability Board, Assessment Methodologies for Identifying Non-Bank Non-Insurer Global Systemically Important Financial Institutions (March 4, 2015), available at http://www.fsb.org/wp-content/uploads/2nd-Con-Doc-on-NBNI-G-SIFI-methodologies.pdf.

[11] As discussed below, JPMAM currently employs swing pricing on the vast majority of our Luxembourg-domiciled UCITS funds, as well as our UK-domiciled Open End Investment Companies. Information on swing pricing can be found in those funds' prospectus at: http://www.jpmorganassetmanagement.lu/EN/dms/JPMorgan%20Funds%20[PRO]%20[GB_EN].pdf (pp. 17-18).

benchmarks are likely to maintain relatively steady allocations to each asset class or sector in their portfolio, a large and growing[12] number of non-traditional and multi-asset funds employ flexible investment approaches across sectors and even asset classes. Such a fund could have a substantially different portfolio than is indicated by a published liquidity metric that is up to five months old.

Additionally, we are concerned that the proposed assessment of days to convert a position to cash is subjective, which could lead very similar funds to disclose different liquidity profiles. Our proposed approach to liquidity classifications will reduce the variability across funds but, particularly for the first year or two, there are likely to be discrepancies in how funds report their liquidity. While the SEC will have the underlying data to identify and calibrate these differences, we are concerned that third party ratings would simply take the funds' own assessments. This could lead to comparisons that disadvantage funds with a more conservative approach to classification, and provide false assurances to investors regarding funds that are more aggressive in their approach to classifications.[13]

With respect to public disclosure of a fund's HLA threshold, we have two concerns. First, as discussed above, we believe liquidity management should be a dynamic and flexible process, and that a fund's HLA threshold may change based on reasonably foreseeable near term market conditions. Thus, a publicly disclosed HLA threshold may be a stale snapshot in time, and potentially not reflective of the fund's actual HLA or portfolio management approach at the time it is being relied upon by an investor. Perhaps more importantly, the public disclosure of such a number could actually *incentivize* investors to redeem quickly at the first indication of potential market stress. Although the HLA threshold is not necessarily a reflection of the actual portfolio, its disclosure may create the perception that a fund has only the enumerated amount of liquidity available to meet redemptions, which could drive investors to redeem before this supposed liquidity runs out.

In sum, we support monthly reporting of liquidity classifications and HLA thresholds to the SEC, which could potentially be shared with other regulators. We also support the proposed disclosure to investors on Form N-1A, and would further support requiring a discussion of liquidity management policies and procedures. However, because we think position-level liquidity classifications are not likely to be useful to investors and could in fact be an inaccurate representation of a fund's current

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[12] Since 2010, AUM in non-traditional bond funds have increased approximately 40% (from $55B in Dec. 2010 to $139B in Nov. 2015); assets in multi-sector bond funds have increased approximately 50% (from $90B in Dec. 2010 to $166B in Nov. 2015); and AUM in multi-asset funds have increased over 60% (from $644B in Dec. 2010 to $997B as of Nov. 2015. These funds typically have flexible investment mandates, and their holdings and liquidity profiles could change substantially over the course of several months.

[13] It should be noted that, even without disclosing funds' liquidity classifications on Form N-Port, third-party data analyzers can and do develop liquidity ratings by imposing their own liquidity metrics on funds' disclosed portfolio holdings. *See, e.g.,* "Press Release: Interactive Data Set to Launch Liquidity Indicators Service," May 18, 2015, *available at* https://www.interactivedata.com/Assets/DevIDSite/PR-2015/Interactive-Data-Set-to-Launch-Liquidity-Indicators-Service.pdf. These metrics are likely to be more comparable, since the service providers are applying consistent liquidity classifications.

portfolio holdings, and because disclosure of an HLA threshold could potentially incentivize first movers, we recommend that the Commission not require such disclosure to the public.

Swing Pricing

JPMAM applauds the Commission's willingness to permit swing pricing for open-end funds. We employ swing pricing on the vast majority of our Luxembourg-domiciled UCITS funds, as well as our UK-domiciled Open End Investment Companies.[14] We believe that, by reducing dilution of the fund as a result of transaction costs, swing pricing is likely to benefit our long-term shareholders.[15]

As a general matter, we support the SEC's proposed approach to swing pricing, including that its use would be voluntary, governed by board-approved policies and procedures, and subject to disclosure and reporting requirements on Forms N-1A and N-CEN. We recommend that the Commission permit, but not require, the consideration of market impact in setting a swing factor, and we suggest more flexibility in the factors for establishing a swing threshold. We also describe several operational obstacles to implementation of swing pricing at this time. Nonetheless, we believe that if the SEC permits the use of swing pricing, the industry will work with its partners in the fund distribution chain to find solutions to the operational concerns. We therefore support the proposal, subject to the following comments.

First, we do not support the proposed *requirement* that a fund's swing factor take into account "market impact costs." We agree that including market impact costs in a fund's swing factor would make swing pricing an even better tool for addressing liquidity risks, because it would charge transacting shareholders for changes to the market value of securities bought or sold as a result of their transactions. However, based on our experience with swing pricing in Luxembourg and the UK, we do not believe there currently exists a conventional or commonly used method for incorporating market impact costs into a swing factor. We believe this would take substantial additional consideration, data, modeling and testing.[16]

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[14] We would be pleased to meet with the Commission or its staff to discuss our experience with swing pricing in more detail.

[15] As part of our annual swing threshold review for these funds, we quantify the dilution saved, in dollars and as a percentage of AUM.

[16] The Proposing Release concedes that "[m]arket impact cost cannot be calculated directly. It can be roughly estimated by comparing the actual price at which a trade was executed to prices that were present in the market at or near the time of the trade." Proposing Release at 187-88, n. 415. Absent some ability to model and predict such costs, we are uncertain as to whether they could be included in a predetermined and periodically reviewed swing factor, or alternatively whether a fund's swing factor would have to be determined on a daily basis, which may not be feasible.

Meanwhile, swing pricing as currently employed, which takes into account such costs as transaction costs, spreads, and taxes such as stamp duties,[17] can still benefit long-term shareholders by reducing dilution, and can act as a disincentive for investors to redeem in times of stress by imposing a charge when the swing threshold is breached. We therefore recommend that the SEC permit swing pricing as currently used, while making the consideration of market impact costs optional for purposes of establishing a fund's swing factor.[18] Over time, we believe the industry would explore ways to incorporate market impact. Funds that employ swing pricing could also be required to describe in their prospectus the costs that are considered in establishing a swing factor, so that investors are aware of their funds' practices.

Secondly, we do not believe a fund's investment strategy, the liquidity of portfolio assets, or the costs associated with transactions should be required considerations for determining a swing threshold. These criteria are important in considering a swing *factor*, which may be set very low for a fund that typically has high liquidity and low transaction costs. To set a threshold, on the other hand, a fund may wish to look primarily at its flows, and determine the amount of flows it wishes to capture with swing pricing to reduce dilution. Even minimal dilution can be impactful over time, and a fund may elect to implement swing pricing, with a low swing factor, to address such dilution. Additionally, fund complexes may prefer to implement swing pricing at the same threshold on the full range of funds, even in cases where the swing factor is low (because transaction costs are minimal), rather than establish different thresholds for each fund. Thus, we recommend that these factors be optional considerations for the determination of a swing threshold.

Finally, as an operational matter with respect to implementation of swing pricing in the US, we are not confident in our ability to determine a fund's net flows in a timely fashion and with sufficient certainty to warrant adjusting the NAV. In the US, we are required to accept shareholder orders until the fund is closed for valuation, *i.e.,* 4 pm. NAVs must be submitted for publication by 6 pm. Meanwhile, trade flows for funds that are sold via third party distributors are generally not available until the early morning of T+1.[19] By contrast, in Luxembourg, we stop accepting orders at 2:30 pm,

[17] *See* "Swing pricing: The J.P. Morgan Asset Management approach in the Luxemburg domiciled SICAVs JPMorgan Funds and JPMorgan Investment Funds," April 2015, available at http://www.jpmorganassetmanagement.de/DE/dms/Swing%20Pricing%20[MKR]%20[IP_EN].pdf.

[18] This would be consistent with the recently released Swing Pricing Guidelines from the Association of the Luxembourg Fund Industry, which includes market impact as an item that *could* be considered when deriving the swing factor. *See* Association of the Luxembourg Fund Industry, Swing Pricing Guidelines, December 2015, available at http://www.alfi.lu/sites/alfi.lu/files/Swing-Pricing-guidelines-final.pdf, at 12.

[19] Indeed, some of those flows, particularly those for 401(k) plans, cannot be calculated until *after* the NAV is submitted. Since 401(k) flows tend to be steady, however, it is possible that they could be estimated with reasonable certainty.

Central European Time, and receive cash projections at 5:30 pm. NAVs are released at 7:15 pm. This timeline is sufficient to analyze cash flows and determine whether to swing the NAV.[20]

We have begun conversations with our distribution partners about the feasibility of obtaining cash flow protections on T, but these discussions are in the early stages. Moreover, we believe such talks are more likely to bear fruit if they are part of an industry call to improve cash flow projections, rather than bespoke arrangements between various fund complexes and distributors. Another potential improvement would be to delay the NAV publication time from 6 pm to 8 pm. We support the industry efforts to resolve these operational issues,[21] and we encourage the SEC to consider how it could engage in such efforts, such as by participating in industry roundtables.

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JPMAM appreciates the opportunity to comment on the Commission's proposed rule. We would be pleased to provide any further information or respond to any questions that the Commission or the staff may have.

Very truly yours,

/s/ George C.W. Gatch

George C.W. Gatch

Cc: The Honorable Mary Jo White, Chair
The Honorable Kara M. Stein, Commissioner
The Honorable Michael S. Piwowar, Commissioner

David W. Grim, Director, Division of Investment Management

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20 We back-tested our cash flow projections versus revised cash flows over three years, and found very high accuracy in the swing pricing determinations (*i.e.,* sufficient to satisfy the SEC's proposed "determination on the basis of information obtained after reasonable inquiry").

21 We concur with the operational challenges described by the Global Association of Risk Professionals in its comment letter on this proposal. *See* Letter from Richard Apostolik, President and CEO, Global Association of Risk Professionals, to Brent Fields, Secretary, Securities and Exchange Commission, dated Jan. 12, 2016, available at https://www.sec.gov/comments/s7-16-15/s71615-33.pdf.