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VIA EMAIL

January 13, 2016

Mr. Brent J. 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 Nos. S7-16-15; S7-08-15

Dear Mr. Fields:

We appreciate the opportunity to comment on the Securities and Exchange Commission's (the "Commission's") above-referenced proposal to require open-end funds to establish liquidity risk management programs and to permit swing pricing by open-end funds on an optional basis (the "Proposal"). The Capital Group Companies is one of the oldest asset managers in the United States. Through our investment management subsidiaries, we actively manage assets in various collective investment vehicles and institutional client separate accounts globally. The vast majority of these assets consist of the American Funds family of mutual funds, which are U.S. regulated investment companies managed by Capital Research and Management Company, distributed through financial intermediaries and held by individuals and institutions across different types of accounts.

As an initial matter, we believe that mutual funds have generally been successful in appropriately managing liquidity risk and we note that many fund organizations, including the American Funds, already employ comprehensive risk management practices. Indeed, we do not believe that there is evidence of a widespread inability, or risk of failure, across the fund industry with respect to funds' ability to meet redemption requests. We believe the few recent failures involved unique circumstances and are primarily attributable to practices that did not have sufficient oversight or controls. However, we support the spirit of the Proposal and the Commission's goal of promoting effective liquidity risk management practices throughout the open-end fund industry, which should help reduce the risk that funds will be unable to meet redemption obligations, particularly for those funds that the Commission notes have dedicated significantly fewer resources to managing liquidity risk in a formalized way. We also strongly believe that the Commission, as the primary regulator of open-end funds, is the appropriate regulator to address these concerns.

In light of the above, we offer the following comments on specific aspects of the Proposal. Section A provides comments on the proposal to require open-end funds to establish liquidity risk management programs, Section B provides comments on the proposal to permit swing pricing by open-end funds on an optional basis and Section C provides comments on the proposed amendments to enhance disclosure regarding liquidity and redemption practices.

A. Liquidity Risk Management Programs

1. **We strongly support the Commission's proposal to require each fund to adopt and implement a liquidity risk management program**

We strongly support the Commission's proposal to require each fund to adopt and implement a liquidity risk management program that is reasonably designed to assess and manage the fund's liquidity risk. As stated by the Commission, a hallmark of open-end funds is that they must be able to convert some portion of their portfolio holdings into cash on a frequent basis because they issue redeemable securities. Although we believe that many funds already employ comprehensive and effective risk management practices to manage liquidity risk, we also acknowledge that there may be funds that have not adopted sufficient practices in this regard, and agree that there are substantial benefits to requiring all funds to address liquidity in a more formalized and consistent way. We believe that such measures will enhance investor protection and mitigate any potential systemic risk to financial stability.

We also agree with the Commission that the requirements of rule 22e-4 should apply to all registered open-end management investment companies (excluding money market funds), regardless of the fund's investment strategy or other factors. While certain funds may be relatively more prone to liquidity risk, we believe that there is benefit to requiring all registered open-end funds to adopt robust and reasonably designed liquidity risk management programs. Indeed, as noted by the Commission, even funds with investment strategies that historically have entailed relatively little liquidity risk could experience liquidity stresses in certain environments.

2. **Although we believe that there is merit to requiring funds to analyze the liquidity of each portfolio position, we are concerned that the specific classification approach set forth in the Proposal may not be workable**

Under proposed rule 22e-4(b)(2)(i), each fund is required to classify each of the fund's positions in a portfolio asset (or portions thereof) into one of six liquidity categories based on the number of days within which it is reasonably determined that the asset could be converted to cash at a price that does not materially affect the value of that asset immediately prior to sale. We agree with the Commission that liquidity is more appropriately evaluated across a spectrum, as opposed to making a binary determination of whether an asset is liquid or illiquid, and also agree that there is merit in requiring funds to analyze the liquidity of each portfolio position. However, we are concerned that the Proposal's six category classification requirements may not be workable.

Most significantly, we note that the proposed classification categories imply a level of precision in making determinations that does not exist. We agree that codifying the factors required to be considered in making liquidity determinations will contribute to more consistency in the quality and breadth of funds' analyses of their portfolio positions' liquidity; however, we are concerned that different funds could classify the liquidity of identical portfolio positions differently. We would emphasize that liquidity is dynamic and that liquidity determinations are inherently uncertain, particularly for debt securities and other instruments that trade over-the-counter. Funds may also vary in how they interpret and weigh the factors required to be considered in making liquidity determinations, which will likely lead funds to assess liquidity for the same assets differently.

In addition, the concept of converting the asset to cash "at a price that does not materially affect the value of that asset immediately prior to sale" is simply too subjective. Markets are volatile, and any trade will typically have some market impact. It is impossible to make a precise judgment about a future price movement before an asset is sold, and it will be up to funds to interpret what "material" should mean in this context. While we support the Commission's goal of ensuring that funds are able to meet redemption requests, we do not believe that funds should be required to make forward-looking predictions relating to market volatility.

For the reasons set forth above, at a minimum, we believe the Proposal should be amended to provide that funds and other applicable persons, including investment advisers and funds boards, will not be liable for liquidity classification determinations that subsequently turn out to differ from actual outcomes to the extent that such determinations were made in good faith. Additionally, we understand that others in the fund industry, including the Investment Company Institute, are submitting comments suggesting various alternatives to the proposed liquidity categories. We encourage the Commission to consider these alternatives in formulating a revised classification requirement that addresses the Commission's goals in a way that raises fewer concerns than the current proposal.

3. **Although we generally support the proposed asset classification factors, the Commission should extend the comment period for the factor requiring consideration of the "relationship of the asset to another portfolio asset" to be conterminous with the comment period for the Commission's pending proposal on the Use of Derivatives by Registered Investment Companies and Business Development Companies**

Proposed rule 22e-4(b)(2)(ii) would require a fund to take nine factors into account, to the extent applicable, when classifying the liquidity of each portfolio position in a particular asset. We support the proposed list of factors set forth in subclauses (A) through (H) of the rule, and agree that requiring funds to consider these factors will encourage effective liquidity assessment across the fund industry and further the goals of the Proposal. However, with respect to the factor set forth in subclause (I), which requires consideration of the "relationship of the asset to another asset", we request that the Commission extend the comment period to be coterminous with the comment period for the Commission's pending proposal on the Use of Derivatives by Registered Investment Companies and Business Development Companies (the "Derivatives Proposal"). In particular, commenters need additional time to consider the guidance that funds should classify the liquidity of assets used for "cover" using the liquidity of the derivative instruments they are covering in light of the proposed rules on asset segregation set forth in the Derivatives Proposal.

4. **We support the aspects of the Proposal requiring funds to assess and manage liquidity risk, including the three-day liquid asset minimum and the codification of existing guidance with respect to 15% standard assets**

We support the aspects of the Proposal set forth in rule 22e-4(b)(2)(iii) that require funds to asses and periodically review liquidity risk, including the list of factors that funds must consider in such assessment and review. We also support the aspects of the Proposal set forth in rule 22e-4(b)(2)(iv) that require funds to manage liquidity risk, including (i) the requirement to determine and periodically review the fund's three-day liquid asset minimum, considering the prescribed list of factors, (ii) the prohibition against acquiring any less liquid asset if, immediately after the acquisition, the fund would have invested less than its three-day liquid asset minimum in three-day liquid assets and (iii) the prohibition, replacing earlier guidance, against acquiring any 15% standard asset if, immediately after the acquisition, the fund would have invested more than 15% of its total assets in 15% standard assets. We agree with the Commission that these aspects of the Proposal will further the Commission's goals by increasing that likelihood that funds hold adequate liquid assets to meet redemption requests without materially affecting the fund's NAV and increasing the likelihood that a fund's portfolio is not concentrated in assets whose liquidity is limited.

5. **Funds boards should not be required to approve specific aspects of the fund's liquidity risk management program and material changes thereto**

Proposed rule 22e-4(b)(3)(i) would require each fund to obtain initial approval of its written liquidity risk management program (including the fund's three-day liquid asset minimum), as well as any material change to the program, from the fund's board of directors, including a majority of directors who are not interested persons of the fund. Although we believe that independent oversight of a fund's liquidity program by the fund board is appropriate, we do not believe that boards should be required to approve specific aspects of liquidity programs, such as the three-day liquid asset minimum.

The Commission notes that directors may satisfy their approval obligations by reviewing summaries of the liquidity risk management program prepared by the fund's investment adviser or others. However, the determinations required to be made in order to establish the fund's three-day liquid asset minimum and other aspects of the fund's liquidity program are technical, fact-intensive and may require day-to-day judgments best left to the fund's adviser. As such, we do not believe it is appropriate to ask fund boards to assume this responsibility and liability. Instead, we suggest that the Commission amend the Proposal so that fund boards would be required to oversee the fund's liquidity program generally, including by receiving written reports at least annually, but that the investment adviser would bear the responsibility for establishing and maintaining each specific aspect of the program. We believe that this structure would facilitate independent scrutiny by the board of directors of the liquidity program, but would also be more in line with the responsibilities of the board of directors in other areas, such as under rule 38a-1 under the Investment Company Act of 1940 (the "1940 Act") (which, as noted by the Commission, does not require a fund board to approve changes to a fund's compliance policies and procedures). Funds would also have more flexibility and could more efficiently modify the three-day liquid asset minimum in reaction to market or other events, as appropriate. We believe this flexibility would be beneficial to funds and shareholders.

6. **We encourage the Commission to consider whether certain funds may be inappropriate for the open-end fund structure**

Failures of mutual funds to meet their redemption obligations have been rare historically. Nevertheless, in addition to requiring open-end funds to adopt liquidity risk management programs, we believe that certain investment strategies may be inherently inappropriate for the open-end fund structure due to objectives and strategies that make daily redeemability challenging. Such funds, which may include those with concentrated distressed debt portfolios and certain alternative funds, are likely more suitable as closed-end funds, interval funds or private funds. We encourage the Commission to more carefully scrutinize such funds before using its authority to facilitate the offering of such funds (i.e., by accelerating the registration of such funds under the Securities Act of 1933).

7. **The compliance date for proposed rule 22e-4 should be 30 months after the effective date for all funds**

The Commission has proposed a compliance date of 18 months after the effective date for larger entities, and 30 months after the effective date for smaller entities, to comply with proposed rule 22e-4. We do not believe that 18 months is sufficient time for larger entities to properly prepare internal processes, policies and procedures and implement liquidity risk management programs that meet the requirements of the rule, and instead suggest a compliance date of 30 months after the effective date for all entities. Although many funds already employ comprehensive programs to manage liquidity risk, those programs likely differ in material respects from the Commission's proposal and will therefore require substantial revisions to infrastructure. In addition to the time required to build out internal systems and processes, we note from our discussions with third-party vendors that such vendors currently do not have analytical capabilities to provide all the requested data.

On top of the time that the vendors will need to expand their capabilities, funds will need time to review vendor methodologies and the quality of the data received to determine the extent to which such data can be used to inform liquidity classifications.

B. <u>Swing Pricing</u>

1. **Although we support swing pricing, we believe that the Commission should delay the effectiveness of rule 22c-1(3) until industry structural issues are addressed**

We strongly support swing pricing as a tool to mitigate dilution of the interests of fund shareholders by passing on the fees and costs stemming from net capital activity to the shareholders associated with that activity. We believe that swing pricing has proven to be beneficial in this regard in certain foreign jurisdictions. However, in order for swing pricing to be successful in the U.S., there are industry structural issues that need to be resolved prior to implementation.

As proposed by the Commission, swing pricing requires the net cash flows for a fund to be known, or reasonably estimated, before determining whether to adjust the fund's NAV on a particular day. Because the deadline by which a fund must strike its NAV may precede the time that a fund receives final information concerning daily net flows from the fund's transfer agent or principal underwriter, the Commission has proposed to permit the person responsible for administering swing pricing policies and procedures to determine whether net purchases or net redemptions have exceeded the fund's threshold "on the basis of information obtained after reasonable inquiry." We request that the Commission delay effectiveness of rule 22c-1(3) indefinitely in order to allow for time to address issues arising from delayed receipt of cash flow information from intermediaries. As alluded to by the Commission, due to operational processes in the U.S., funds typically receive cash flow information from intermediaries, such as broker-dealers, fund platforms and retirement plans, subsequent to the deadline by which a fund is required to strike its NAV, and often not until the following morning. Given that the majority of fund shares in the U.S. are sold through intermediaries, such flows may represent a substantial portion of a fund's daily flows, and funds therefore may not have reliable information on which to determine whether the swing threshold has been breached. This could result in a fund swinging its NAV in the wrong direction, e.g., if the data known at the time NAV is struck indicates that net cash flows into the fund are likely to exceed the swing threshold, but data received later shows that the fund actually suffered net outflows in an amount exceeding the swing threshold. Conversely, we note that funds that have successfully implemented swing pricing outside the U.S. operate in jurisdictions that permit them to obtain accurate estimates or actual information on capital flows prior to the time that funds must calculate their NAV.

If the swing pricing rule were to become effective upon the date of the final rule, as currently proposed, funds wishing to secure a competitive advantage could choose to implement swing pricing ahead of more prudent funds that recognize the need for changes to operational processes in order to receive sufficient information about fund flows at the time NAV is struck. Moreover, a delay in effectiveness would ensure that funds are prudent in taking the necessary time to work through any other legal, business and operational issues relating to implementation and would not be disadvantaged against funds that choose to adopt it more quickly.

2. **The Commission should require intermediaries to provide fund flow estimates prior to the deadline by which a fund must strike its NAV**

The Commission has also suggested that each fund arrange for interim feeds of flows from its transfer agent or distributor in order to reasonably estimate its daily net flows or implement policies to encourage effective communication channels between the persons charged with implementing the fund's swing pricing policies and procedures, the fund's investment professionals, and personnel charged with day-to-day pricing responsibility. However, we do not believe that these proposed solutions will be effective. In order to create a level playing field for all funds, we instead urge the Commission to adopt rules requiring intermediaries to provide cash flow information prior to the deadline by which a fund is required to strike its NAV. Without this requirement, intermediaries may be incentivized not to provide timely cash flow information because such information would increase the likelihood of triggering a swing. Intermediaries would also be likely to favor and provide flow information sooner to larger clients, which would give certain funds an advantage over others. We note that some intermediaries do provide intra-day estimates to advisors of anticipated flows today, so it is possible, but other intermediaries may not do so unless required.

3. **The Commission should clarify that inaccuracies in estimating net cash flows will not constitute a NAV error or otherwise give rise to liability**

As discussed above, the Commission has proposed to permit the person responsible for administering swing pricing policies and procedures to determine whether net purchases or net redemptions have exceeded the fund's threshold "on the basis of information obtained after reasonable inquiry." The Commission should amend the Proposal to provide that, so long as such person has a process for reasonably estimating flows at the time NAV is struck, inaccuracies in estimating net cash flows will not be considered a NAV error for the fund, nor give rise to any liability for the fund, such person, the fund's adviser or the fund's board of directors. We believe that this would be warranted given that fund flows from intermediaries are often delayed and that funds may be estimating NAV based on only portions of flow data.

4. **The Commission should explicitly provide that a fund may consider market movements in determining whether the fund's level of net purchases or net redemptions has exceeded the fund's swing threshold.**

The Commission should explicitly provide that a fund may consider market movements in determining whether the fund's level of net purchases or net redemptions has exceeded the fund's swing threshold. For example, if the fund determines based on historical data that a drop in the applicable equity or debt market over the course of the day is correlated with investors selling fund shares, the fund should be permitted to take this information into account in its reasonable estimation of whether the fund's swing threshold has been exceeded. Given that most funds will only have portions of flow data at the time they are estimating whether the fund's swing threshold has been exceeded, we believe that permitting consideration of the impact of market movements based on historical trends would lead to more accurate swing determinations.

5. **Fund boards should not be required to approve specific aspects of the swing pricing policies and procedures**

Under proposed rule 22c-1(3)(ii)(A), a fund's board, including a majority of the fund's independent directors, would be required to approve the fund's swing pricing policies and procedures (including the fund's swing threshold, and any swing factor upper limit specified under the fund's swing pricing policies and procedures), as well as any material changes thereto. While we agree that a fund's board should be required to approve the fund's general swing pricing policies and procedures, we do not believe that boards should be required to approve specific aspects of such policies and procedures, such as the fund's swing threshold and any swing factor upper limit, and that these approvals should instead be established by the investment adviser, who has closer knowledge and visibility to the dynamics of the investment-related factors considered in setting the thresholds and limits. Although we believe that fund boards should be given visibility to such determinations through written reports, we do not believe that it is appropriate to ask the fund's board to bear the responsibility and liability for approving specific technical aspects of the swing pricing policy and procedures. Given that the determination of the right swing threshold and whether a swing factor upper limit is appropriate involve complex analysis and will vary for different funds, we believe the investment adviser or other officers responsible for administering the swing pricing policies and procedures are better equipped to make this determination than the fund board.

6. **We support the requirement that the determination of the swing factor must be reasonably segregated from the portfolio management function of the fund**

The Commission has also asked whether commenters agree that the determination of the swing factor should be reasonably segregated from the portfolio management of the fund, as currently required by proposed rule 22c-1(a)(3)(ii)(B). We agree with the Commission that, in determining the swing factor, independence from portfolio management is important because the incentives of portfolio managers may not always be consistent with determining a swing factor that most effectively prevents dilution of existing shareholders' interests in the fund.

C. <u>Disclosure and Reporting</u>

1. Funds should not be required to file agreements related to lines of credit as an exhibit to the registration statement.

The Commission is proposing to amend Item 28 of Form N-1A to require a fund to file as an exhibit to its registration statement any agreements related to lines of credit for the benefit of the fund. Although the Commission would not require funds to disclose the fees relating to such agreements, lines of credit are often heavily negotiated and there are other provisions in such agreements that lenders and funds may wish to keep confidential for business reasons, such as representations and warranties. In addition, such agreements are often extremely lengthy and are not user friendly. For these reasons, we instead suggest that funds be required to summarize the material provisions of such agreements in the fund's Statement of Additional Information, similar to the disclosure regarding such agreements that is proposed to be required on Form N-CEN. We believe that providing summary disclosure of the material provisions of a line of credit would be a more effective way to provide the Commission, investors and other market participants with relevant information regarding such arrangements.

2. Funds should not be required to publicly disclose asset-by-asset liquidity classifications and whether each portfolio asset is a 15% standard asset on Form N-PORT

The Commission proposes to amend proposed Form N-PORT to require a fund to report its liquidity bucket classification of each portfolio asset, the fund's three-day liquid asset minimum, and whether each portfolio asset is a 15% standard asset. As noted above in Section A, while we believe there is merit to requiring funds to analyze the liquidity of each portfolio position, we question whether the proposed classification approach is workable. We urge the Commission to give consideration to alternative classification approaches suggested by the Investment Company Institute and others. In addition, while we do not object to providing classification information to the Commission, we believe it would be detrimental to provide asset-by-asset liquidity classifications to individual investors. Instead, we suggest that such information be provided to investors on an aggregate level for the entire fund (i.e., on a percentage basis).

Our primary concern with the current proposal is that providing asset-by-asset classifications will be confusing and misleading to investors. As noted above, liquidity determinations are fluid and involve considerable judgment, thus potentially leading funds to classify the same assets differently. As currently proposed, Form N-PORT would not allow for any explanation to investors regarding the nature of the data and its limitations, therefore giving investors a false sense of precision concerning, and an incomplete picture of, the data. Such a presentation would directly conflict with the Commission's goal of providing informative liquidity information to investors. We also disagree with the Commission's view that public disclosure will lead to more consistent liquidity determinations across funds, particularly given that liquidity determinations will vary based on the size of the positions and other factors.

Moreover, we believe that there are potential market impacts if the information were to be publicly disclosed. For example, to the extent funds categorize securities in the less liquid buckets (e.g., greater than 15 calendar days), we believe dealers will be less inclined to make markets in such securities, which will actually worsen liquidity. In addition, public disclosure could incentivize "window dressing" and market disruption at period ends when entities know positions will need to be disclosed.

We are also concerned that public disclosure in the currently proposed form could unduly impact capital markets and the ability of issuers, and in particular smaller companies to raise capital if mutual funds became disinclined to invest in such companies out of fear that categorizing the issuer's securities in a less liquid category would create a negative perception of the fund.

The Commission should also be aware that reporting requirements related to the proposed classification requirements may be procyclical and yet the timing of public disclosure is unlikely to keep pace with actual changes in market liquidity for both better and worse. We are concerned that this potential timing mismatch will create unnecessary noise in the market and confusion for mutual fund shareholders. We believe investors would be much better served by aggregate portfolio-level information showing appropriate high-level reflections of liquidity. This would provide investors with relevant and useful information regarding the liquidity profile of a fund, without causing confusion or creating the false impression that determinations with respect to specific assets are objective or fixed in time.

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On a final note, we applaud the Commission not only in its efforts to promote effective liquidity risk management throughout the open-end fund industry, but also in advancing its broader set of recent initiatives, of which the current Proposal is a part, designed to strengthen and modernize the regulatory scheme. These initiatives include the Commission's proposed rules to modernize and enhance reporting and disclosure by investment companies and investment advisers and the Commission's proposed rules to improve the regulatory framework regarding derivatives. We also understand that the Commission is considering proposing new requirements for stress testing by large investment advisers and investment companies. Stress testing of fund portfolios to consider unusual market conditions should complement the rule proposal requiring funds to establish liquidity risk management programs. We believe that this set of comprehensive initiatives will strengthen the open-end fund industry, reduce risk and provide increased investor protection. In formulating final rules, we encourage the Commission to review all of these proposals holistically and to consider how they will work together to strengthen the overall regulatory framework.

We truly appreciate the opportunity to comment on the Proposal. If you have any questions regarding our comments, please feel free to contact Rachel V. Nass at ([redacted]-[redacted].

Sincerely,

Paul F. Roye
Senior Vice President
Capital Research and Management Company

Rachel Nass

Rachel V. Nass
Counsel
Capital Research and Management Company

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