December 13, 2022

Ms. Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549

Re: File No. S7-26-22
Open-End Fund Liquidity Risk Management Programs and Swing Pricing; Form N-PORT Reporting

Dear Ms. Countryman:

I appreciate the opportunity to comment on the Securities and Exchange Commission's (the "Commission") proposal on amendments to current rules for open-end management investment companies regarding liquidity risk management programs and swing pricing (the "Proposal).[1] I specifically write to comment on the proposed changes to Rule 22c-1 under the Investment Company Act of 1940 (the "1940 Act") that would require all registered open-end management investment companies to engage in swing pricing under certain conditions and the effects the proposed changes would have on small individual investors like myself.[2] While I support the Commission's attempt to offset dilution that may occur when there are large scale redemptions or purchases in an open-end fund, swing pricing creates an even larger problem and results in increased harm to investors. Instead of proceeding with the proposal to require all open-end funds to engage in swing pricing, the Commission should implement a liquidity fee and such fee should only be imposed on redeeming or purchasing investors.

I. Effects of Swing Pricing on Investors

The Proposal defines swing pricing as a process of adjusting a fund's current net asset value ("NAV") when certain conditions are met in an attempt to pass on transaction costs stemming from shareholder inflows or outflows to the shareholders engaged in that activity.[3] Further, the Proposal states that trading activity associated with purchases and redemptions may impose costs on the funds and such costs are currently borne by non-transacting shareholders.[4] The Commission believes that imposing costs associated with net purchases or net redemptions on the shareholders who are purchasing or redeeming from the fund at that time will more fairly allocate costs and overall increase the fairness in the market.[5]

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[1] SEC Release No. 33-11130; IC-34746 (Nov. 2, 2022) ("Release"), available at https://www.sec.gov/rules/proposed/2022/33-11130.pdf.
[2] This letter was prepared by the author in her personal capacity. The opinions expressed in this letter are the author's alone and do not reflect the view of her employer.
[3] Release at 93-94.
[4] Release at 94.
[5] Release at 94-95.

How much of an adjustment a fund would make to its NAV would be determined by a "swing factor." The proposed rule would require the fund to make a good faith estimate of the costs it may incur "if it purchased or sold a *pro rata* amount of each investment in its portfolio to satisfy the amount of net purchases or redemptions."[6] In the case of net redemptions (redemptions exceeding 1% of net assets), a fund's NAV would swing down in the amount of the swing factor. In the case of net purchases, (purchases exceeding 2% of net assets) a fund's NAV would swing up in the amount of the swing factor. The size of the swing factor depends on the following three factors: (1) spread costs; (2) brokerage commissions, custody fees, and any other charges, fees and taxes associated with portfolio investment purchases; and (3) the market impact.[7]

Swing pricing would have the result of subjecting all investors transacting with a fund on a specific day to the costs imposed on the fund by a few investors engaging in large transactions, creating an unfair disadvantage to smaller shareholders. For example, on a day that a large investor purchases a significant number of shares constituting net purchases, the NAV of the fund would be swung upward, and smaller investors would be subjected to a NAV that is artificially increased and would incur extra costs for making the mistake of buying shares on the same day as a large investor. Additionally, any redeeming shareholder would obtain a windfall over what the NAV should be on trading day due to the swung NAV being artificially increased. The opposite situation is just as harmful. On a day a large investor redeems a significant number of shares constituting net redemptions, the NAV of the fund would be swung downward, and smaller investors would receive less for their redemptions than the true underlying NAV of the fund. Additionally, any investor making purchases on that day would obtain a windfall due to the swung NAV being artificially lower than the true underlying NAV.

The Commission argues that swing pricing is an important tool to reduce the potential for dilution of investors who are not currently transacting in the fund's shares. This may be true, but such a tool should not come at the cost of other, smaller investors—the very ones the Proposal is attempting to protect.

Additionally, the Proposal may have the effect or driving investors away from open-end funds in favor of other products, including exchange-traded funds ("ETFs"), which would not be subject to the proposed mandatory swing pricing.[8] With fewer investors, it may be harder for a fund to achieve economies of scale. Many open-end funds reflect economies of scale through breakpoints in advisory fees. If the economies of scale are not achieved and the breakpoints do not kick in, investors will face higher advisory fees, ultimately resulting in further financial harm to the investor.

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[6] Release at 116.

[7] Release at 118.

[8] Release at 93; *see also* Hester M. Peirce, Commissioner, SEC, Closing Act: Statement on Proposed Open-End Fund Liquidity Risk Management Programs and Swing Pricing; Form N-PORT Reporting (Nov. 2, 2022), available at https://www.sec.gov/news/statement/peirce-statement-open-end-funds-110222 ("Dilution may occur and is more likely in volatile times, but the solution we are proposing today may cost fund investors more than the dilution does. We have other options. First, investors concerned about dilution can invest in ETFs.").

II. Alternatives to Swing Pricing

The Commission considered five types of liquidity fees as potential alternatives to swing pricing, but ultimately decided not to propose any of the five. First, the Commission considered a dynamic liquidity fee that could "be equivalent to swing pricing from the point of view of the transacting investor."[9] The dynamic liquidity fee could charge transacting investors with the estimated trading, spread and market impact costs associated with their purchases or redemptions, "allowing remaining shareholders to recoup these costs and mitigate dilution."[10] The Commission stated that such fee may be more fair to redeeming investors and "would be more transparent regarding the liquidity costs transacting investors are charged."[11] However, the Commission argued that a dynamic liquidity fee could be more operationally challenging to implement because a fund would have to rely on intermediaries to pass the liquidity costs on to transacting investors whereas, with swing pricing, a fund could pass liquidity costs directly on to redeeming or purchasing investors via adjustments in the NAV, with intermediaries receiving the price at the end of the trading day.[12]

I disagree with the Commission's view that a dynamic liquidity fee could be more operationally challenging to implement than swing pricing. In both instances, a fund would need to work with its intermediary, either to tell the intermediary the price of the fund or to request that the intermediary charge a liquidity fee. Further, charging a liquidity fee, as the Commission recognizes that some funds already do, would be less of an operational challenge than swing pricing because implementing swing pricing requires funds to completely overhaul their methods of calculating NAV. Not only does this impose large operational hurdles to fund complexes, but also requires investors to understand an entirely new system when they are already likely familiar with charging of fees (*e.g.*, sales loads). Thus, I believe the Commission should reconsider swing pricing in favor of a dynamic liquidity fee.

Additionally, the Commission considered implementing "a simple fee framework that would require funds to charge a set fee of a specified percentage of the transaction," designed to either apply for all investor transactions, apply if redemptions or subscriptions exceed certain thresholds, or apply only to redemptions or purchases.[13] The Commission stated that a set fee framework "could reduce the operational burdens imposed on funds" because it would not require that a fund receive full order flow data before determining its NAV.[14] However, the Commission was concerned that a set fee could "lead funds to over- or under-charge transacting investors because the trading costs a fund experiences for a given level of net redemptions or subscriptions may vary nonlinearly."[15]

[9] Release at 349.
[10] *Id.*
[11] Release at 350.
[12] Release at 350-51.
[13] Release at 352.
[14] *Id.*
[15] *Id.*

I agree with the Commission's view that a set fee may be less effective than swing pricing at mitigating dilution. If a fund were to charge a 1% set fee any time redemptions or purchases exceed certain thresholds, the fee may be smaller than the actual liquidity costs, resulting in damage to the existing shareholders whose shares will be diluted to cover the remaining liquidity costs. Conversely, the fee may be larger than the actual liquidity costs, resulting in damage to the redeeming or purchasing shareholder. Thus, I do not believe that a set fee is a fair and reasonable option.

Next, the Commission considered a dynamic fee that responds to market conditions "such as bid-ask spreads or other known transaction costs associated with trading underlying investments, but are not tailored to the order flow a fund receives on a given day."[16] The Commission states that under such a fee structure, a fund could charge a liquidity fee on both redemptions and purchases that reflects the estimated costs of buying and selling the fund's underlying assets, excluding market impact.[17]

I believe that a dynamic fee that responds to market conditions is a good alternative to swing pricing. Charging a purchasing or redeeming investor the added costs of buying or selling a fund's underlying assets would take most of those costs off shareholders who are not transacting in the fund, thus reducing dilution. The fee may not be perfect, as it relies on estimates of trading costs and does not consider the potential market impact of a transaction, but it at least mitigates dilution and would not require funds and shareholders to implement and understand an entirely new pricing system. Thus, I believe a dynamic fee that responds to market conditions should be considered preferable to swing pricing.

As another alternative, the Commission considered a liquidity fee that would only apply under certain conditions, "such as when trading costs are significantly above those typically experienced."[18] The Commission stated that while this approach may be less costly and less operationally burdensome for funds to implement, it may not always result in a benefit to investors because if dilution during normal times accumulates to a significant amount over time, fund investors would have no protection against it.[19] Additionally, the Commission was concerned that investors may be able to predict when a fund is moving closer to the fee trigger and may preemptively redeem their shares to avoid the fee, which could exacerbate the first-mover advantage and contribute to further fund stress.[20]

I echo the Commission's concern that such a fee could potentially create a risk for a run on funds and exacerbate any stress the fund was already under. In fact, this was seen in March 2020 when investors began redeeming out of money market funds to avoid the implementation of a redemption fee or gate.[21] Thus, I do not believe that a liquidity fee that would only apply in times

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[16] Release at 353.
[17] *Id.*
[18] Release at 354.
[19] *Id.*
[20] *Id.* at 354-55.
[21] *See* Money Market Fund Reforms, SEC Release No. IC-34441 (Dec. 15, 2021), available at https://www.sec.gov/rules/proposed/2021/ic-34441.pdf.

of increased trading costs would be an appropriate alternative to swing pricing or an effective anti-dilution tool.

Lastly, the Commission considered a liquidity fee only for funds that are not primarily highly liquid.[22] This fee would require funds that "hold less than an identified percentage of their portfolio in highly liquid assets" to impose a fee during periods of increased trading costs.[23] The Commission was concerned, however, that this type of liquidity fund may affect competition in open-end funds as investors may move to investments that are primarily highly liquid to avoid fees in funds that are not.[24]

I do not share the Commission's concerns around competition. Funds that are not primarily highly liquid are often invested in underlying securities that, while they may take longer to convert to cash, provide potential increased returns over products that invest ins underlying securities for which there is a readily available market. Thus, I believe investors will continue to be drawn to products that may not be primarily highly liquid, even if those products may come with additional fees.

III. Conclusion

In conclusion, the Commission should not proceed forward with the proposal to require swing pricing for open-end registered investment companies and instead should allow funds to use liquidity fees as anti-dilution tools. Swing pricing creates an unfair disadvantage to smaller investors who happened to redeem or purchase shares of a fund on a day in which there are net redemptions or purchases. This may drive investors away from these products, making it harder for the fund to achieve economies of scale, further increasing the cost of such funds to investors. In lieu of swing pricing, the Commission should adopt a liquidity fee framework—specifically, a dynamic liquidity fee or a liquidity fee for funds that are not primarily highly liquid. These fees will act as an appropriate anti-dilution tool and will mitigate any adverse effects on investors who remain invested in the fund or are not transacting with the fund at levels that would put a strain on the funds.

Thank you for the opportunity to submit this letter and for your consideration of these comments.

Sincerely,

/s/ Jocelyn Near
Jocelyn Near

[22] Release at 355.
[23] *Id.*
[24] Release at 356.