February 8, 2023

Ms. Vanessa A. Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC
20549-1090

Re: **Open-End Fund Liquidity Risk Management Programs and Swing Pricing; Form N-PORT—Comments on Proposal to Mandate Swing Pricing and a Hard Close [(File No. S7-26-22)]**

Dear Ms. Countryman:

The Independent Directors of the PGIM Retail Funds[1] (the "Funds") appreciate the opportunity to comment on the proposal made by the Securities and Exchange Commission's (the "Commission" or "SEC") to require swing pricing by open-end funds (the "Proposal"). We have never before submitted a comment letter but feel so strongly about the Proposal that we are compelled to weigh in. We are concerned.

While we recognize the Commission's desire to address dilution associated with investor redemptions, we are confused by a Proposal that fails to quantify the issue of dilution in the industry. We also worry that the negative impacts the Proposal would require have not been sufficiently studied or considered. Simply put, the Proposal would disadvantage our Fund shareholders. In fact, we believe it would cause irreparable harm. Given the unique position of independent directors as "watchdogs for the interests of fund shareholders,"[2] we hope you will take our comments to heart. We support any initiative that protects fund shareholders *if* a cost-benefit analysis demonstrates that it will yield greater good than harm. We do not believe the Proposal meets this threshold.

A. First Principles

1. What is the problem?

Any proposal from the Commission, particularly one as significant as this one, should carefully and methodically make the case for why reform is needed. As published, the Proposal fails to provide any hard data to substantiate the idea that dilution is a serious problem in the fund industry. Whatever the Commission's strategies might be for addressing dilution, the first step must be to present evidence of the problem.

[1] The PGIM Retail Funds Complex is comprised of 86 open-end funds, nine ETFs, and $163 billion in assets under management as of December 31, 2022.
[2] Investment Company Governance, 70 Fed. Reg. 39390, 39397 (July 7, 2005).

2. Will the solution benefit investors more than the problem purportedly harms them?

When a Commission initiative includes the phrase "[w]e are not able to quantify many of the costs associated with the propos[al]," alarm bells sound.[3] Our Fund shareholders should not be faced with regulatory initiatives of undeterminable costs. We find it unacceptable that the Commission has issued a Proposal that acknowledges the lack of "granular data" and "operating costs" needed to quantify the expense of implementation.[4] As fiduciaries of the very people who are likely to bear the costs, we urge the Commission spend the time to quantify them.

3. Are investors better off in less regulated products or with fewer choices?

We believe the answer is "no." In its Proposal, the Commission acknowledges that it cannot "predict the number of investors that would choose to keep their investments in the mutual fund sector nor the number of investors that would exit mutual funds and instead invest in other fund structures such as . . . CITs."[5] Is the Commission really putting forth potential reforms that would drive investors out of the type of product that is regulated precisely to protect them? The Proposal also recognizes that investors could replace mutual fund holdings with those of ETFs and closed-end funds. We are puzzled by any proposal that would cause investors to flee the most popular and largest segment of the registered fund landscape when no issues with dilution within that segment have been articulated. Further, we cannot support a Proposal that would cause investors to have fewer rather than more choices.

4. Usurpation of Director Business Judgment: Second Guessing

From time to time, the Commission has pursued regulatory initiatives to strengthen the hand of independent directors. In the last few decades, we have been given an arsenal of tools to represent our Fund shareholders.[6] Concurrently, more and more responsibility has been given to us in recognition of our effectiveness and role as "watchdogs" for investors.[7] The Proposal, however, contradicts this trend. Directors currently have the ability to use swing pricing and we have determined not to do so. The Commission notes this in its Proposal as if that is the problem: that no one has used swing pricing. Why is that a concern? Shouldn't this fact be evidence that those of us who are specifically charged with unbiased oversight of shareholder interests do not believe swing pricing to be a good option for our Fund shareholders under current circumstances? In fact, before issuing its Proposal, it would have been prudent for the Commission to more fully understand why swing pricing has not been implemented. Perhaps some directors have concluded

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[3] Open-End Fund Liquidity Risk Management Programs and Swing Pricing, 87 Fed. Reg. 77172, 77256 (Dec. 16, 2022).

[44] *See id*. ("[W]e do not have granular data on the current practices and operating costs for all funds, which might allow us to estimate how their systems would change as a result of the proposed swing pricing requirement.")

[5] *Id*.

[6] *See*, *e.g.*, the requirements outlined in the Role of Independent Directors of Investment Companies, 66 Fed. Reg. 3734 (Jan. 16, 2001) and Investment Company Governance, 69 Fed. Reg. 3472 (Jan. 23, 2004).

[7] *See*, *e.g.*, recent rulemaking that incorporates director oversight, including Use of Derivatives by Registered Investment Companies and Business Development Companies, 85 Fed. Reg. 83162 (Dec. 21, 2020) and Investment Company Liquidity Risk Management Programs, 81 Fed. Reg. 82142 (Nov. 16, 2016).

that dilution is not a particular concern for their fund group. Or maybe others have concluded that swing pricing is not as helpful as it is detrimental to investors. The fact is, there could be a myriad of excellent reasons. Therefore, the Commission should explore the reasons why swing pricing has not been pursued. Instead, it has assumed that because swing pricing has not been voluntarily implemented, it must now be required. In reaching this conclusion, the Commission has substituted its judgment for that of independent directors. This is contrary to what the Investment Company Act envisions and what the Commission's own actions over the last 25 years suggest.

B. Substantive Issues

1. Hard Close Harms Intermediated Investors

A seminal feature of open-end funds is the promise of a net asset value ("NAV") struck once the markets close on the day an investor places an order for the purchase or sale of fund shares. This is not only a hallmark of mutual funds, but a key element of the most democratized form of investment: regardless of how or where someone buys or sells their fund shares, all investors are treated exactly the same as they add to or decrease their fund holdings. Over the years and as financial intermediaries have proliferated, the Commission has recognized the importance of such equal treatment by allowing intermediaries to send customer orders to fund groups after markets close. Those orders have received the market-close fund NAV so long as they were placed prior to the close and were processed prior to the markets opening on the following day.[8] Under the Proposal, intermediaries would have to aggregate and process all orders prior to 4:00 p.m. Eastern time so they could get the orders to our Funds by that time. We understand that numerous intermediaries, particularly when dealing with investors on the West Coast or with retirement plans, would have to impose mid- or late-morning order cut off times. This would force our intermediated Fund shareholders to commit to an investment decision well before any of our direct investors do. In essence, the Commission is proposing to eliminate the equal treatment of our Fund shareholders, thereby decimating one of the pillars of mutual fund investing: a Fund treats all of its investors equally.

2. Shareholder Exchanges in Peril

Today, intermediaries enable shareholders that hold mutual fund shares in multiple fund families and in multiple funds within the same fund family to exchange shares. This is possible because intermediary orders can be processed, batched, and netted after the close of markets and still receive the market-close NAV. The Proposal would deprive intermediated shareholders from a service they have come to expect. Instead, one part of the exchange would have to be processed on the first day and the second part on day two. This means that the shareholders who buy our Funds through intermediaries would not only lose the efficiency of same-day exchanges, but they would be subject to market risk for an additional 24 hours. That exposure seems entirely unnecessary and unfair. It is certainly inequitable.

3. Investors Transacting at Disparate NAVs

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[8] *See* Staff Interpretive Positions Relating to Rule 22c-1, Investment Company Act, Release No. 5569 (Dec. 27, 1968) (Rule 22c-1 "contemplates that the time of receipt of the order by the retail dealer is controlling" for purposes of determining the price obtained by the dealer).

The Proposal continues to chip away at key features of shareholder equality by setting forth a swing pricing regime that yields arbitrary and unbalanced results. On days on which a Fund experiences net redemptions, the NAV would have to be "swung down," and redeeming shareholders will receive a price lower than NAV for their shares. The Commission's premise is that this will "reduce the dilution of non-transacting fund shareholders by charging redeeming and subscribing investors the trading costs they impose on a fund."[9] This "swung-down NAV" would be triggered by any amount (even a single dollar) that puts the fund in net redemptions. One of the many issues with this scheme is that, because the lowered NAV would be applicable to all investors, those who are purchasing shares on a day of net redemptions would be buying at a discount. Similarly, the proposed swing pricing mechanism would "swing up" the NAV on days on which net purchases exceed 2% of a fund's net assets. Redeeming shareholders on such a day would receive a price higher than what the fund's holdings are worth. Luck would surely favor some and disadvantage others on any given day. Investors who may have been long-term holders of our Fund shares, who may be saving for retirement or college, and who one day have to redeem them or need to purchase more shares would be subject to the vagaries of what other investors choose to do that day. The Commission is proposing to replace the rigor, predictability, and equity of our current NAV striking regime with one that resembles a game of chance.

4. Misleading Performance Metrics

We are concerned that the use of swing pricing will result in the publication of misleading fund performance figures. Because swing pricing allows a fund to adjust its price above or below the fund's per-share NAV, over time, these adjustments could artificially inflate or dampen fund reported performance. Instead of making investment decisions based solely on the performance of fund investments, net of costs, investors would be influenced by the idiosyncrasies of a fund that experiences swings in asset flows. The Commission has historically sought to simplify disclosures, to wit, it often revisits whether prospectuses are in "plain English."[10] This Proposal goes in the opposite direction. It would obfuscate important data, introduce uncertainty, and make it more difficult for investors to comparison shop among funds. The discrepancies that fund flows could have on reported performance would certainly muddle the landscape.

5. Impossibly Complicated Disclosures

Given the complexity of swing pricing mechanics, including but not limited to the calculation of swing pricing thresholds, swing factors and market impact costs, the Board is concerned that disclosure of these elements will create confusion for shareholders. Today's calculation of a NAV is fairly easy to explain and understand. The Proposal introduces complications that prospectus disclosures cannot possibly explain. The most a prospectus could realistically communicate well

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[9] Open-End Fund Liquidity Risk Management Programs and Swing Pricing, 87 Fed. Reg. at 77236.

[10] In 1998, the Commission adopted Rule 421(d) of the Securities Act (the "Plain English Rule"), which requires issuers of securities to write the cover page (front and back, inside and outside), summary and risk factors section of prospectuses in "plain English." The Commission, at the same time, amended Rule 421(b) to provide further guidance on how to prepare a prospectus to meet the pre-existing rule that a prospectus be "clear, concise and understandable." In 2009, the Commission adopted a rule providing for mutual fund summary prospectuses to be written in plain English. Item 503 of Regulation S-K.

would be the bottom line: a warning to investors that they may or may not receive the calculated NAV on a particular day and that the NAV's fluctuation will depend on the day's asset flows.

6. Reduction of Shareholder Choice and Increased Costs

The requirement for a hard close would fundamentally change the buying and selling experience of retail investors who invest in mutual funds through retirement plans or through intermediaries. Although the Commission assumes that retirement plans and intermediaries would change their systems to accommodate the hard close, we believe a more likely scenario would be the replacement in retirement plans and intermediary platforms of mutual funds with other investment vehicles that do not necessitate these system changes. It is reasonably foreseeable, for example, that CITs could replace mutual funds in many platforms. That would be an easier and less expensive way for platforms to deal with the hard close retirement. If this is the case, and we expect it to be, then the Commission will have failed to address the problem it has set out to solve: investor dilution in open-end funds. The Commission will have succeeded only in pushing this problem off of mutual funds and onto CITs, with no improvement and less regulation for investors. If the effect of the Proposal is the widespread shift of money from mutual funds to CITs, there exists no justification for regulatory action in the first place. The solution to mutual fund investor dilution is not the regulatory cannibalization of mutual funds.

Even if platforms do change their systems, we expect the costs of overhauling operations would find their way to fund shareholders. Either way, it would be a lose-lose proposition for our investors: their investment choices could include less regulated products or include the same products at a higher cost.

C. Conclusion

Our Board is concerned that in the pursuit of a solution to a theoretical problem, the Commission has overlooked the need to establish that the problem exists in the first place. It may be that dilution is a serious problem in the industry, but we have yet to see data that substantiate that premise. Even if dilution is rampant and investors are being harmed, the solution to the problem should not do more harm than the problem itself. Creating inequities among investors, uncertainty in fund NAVs, confusion in performance data, disclosures that are less clear, and frameworks in which investor money flows into less regulated vehicles, all with the certainty that shareholder costs will rise and that they cannot be quantified seems fairly disastrous to us. We expect a more thoughtful evaluation from the Commission. We encourage the Commission to convene working groups of relevant industry participants to consider the nature and extent of dilution in the fund industry as well as the feasibility and implications of swing pricing and the hard close requirement. If a problem does exist, we are confident that working with the industry, the Commission can develop a set of thoughtful and appropriate remedies that are not worse than the ailment.

Sincerely,

/s/ Keith F. Hartstein
Keith F. Hartstein, Independent Board Chair, PGIM Retail Funds

On behalf of:

Ellen S. Alberding
Kevin J. Bannon
Linda W. Bynoe
Barry H. Evans
Laurie Simon Hodrick
Brian K. Reid
Grace C. Torres

cc: The Hon. Gary Gensler, Chair, U.S. Securities and Exchange Commission
The Hon. Hester M. Peirce, Commissioner, U.S. Securities and Exchange Commission
The Hon. Caroline A. Crenshaw, Commissioner, U.S. Securities and Exchange Commission
The Hon. Mark T. Uyeda, Commissioner, U.S. Securities and Exchange Commission
The Hon. Jaime Lizárraga, Commissioner, U.S. Securities and Exchange Commission
Mr. William A. Birdthistle, Director, Division of Investment Management, U.S. Securities and Exchange Commission