FEBRUARY 14, 2023

Via email to: rule-comments@sec.gov

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

RE: File No. S7-26-22 – Request for comment on Release No. IC-34746, Open-End Fund Liquidity Risk Management Programs and Swing Pricing; Form N-PORT Reporting

Dear Ms. Countryman:

On behalf of Allspring Global Investments ("Allspring"), we appreciate the opportunity to respond to the request by the U.S. Securities and Exchange Commission ("Commission" or "SEC") for comments on the SEC's proposal to revise the liquidity risk management program requirements applicable to mutual funds and exchange-traded funds and to require swing pricing by mutual funds (the "Proposal").[1]

Allspring[2] is the sponsor of the Allspring Funds, a registered fund complex which offers mutual funds, closed-end funds and money-market funds to retail and institutional investors.[3] As members of the Investment Company Institute ("ICI") and the Asset Management Group of the Securities Industry and Financial Markets Association ("SIFMA AMG"), we have participated in the drafting of their comment letters on the Proposal and endorse the views expressed therein. We write separately to offer the Commission data showing that, with respect to certain mutual funds that invest principally in small cap equity securities, the cumulative impact of the Proposal's proposed changes to liquidity risk management ("LRM") program parameters (i) would lead to results for such funds that are inconsistent with our understanding of their liquidity profiles both in normal market conditions and in stressed markets like those experienced in March 2020 (a time period which has in large part motivated the Proposal) and (ii) would require changes to such funds that are both unnecessary from a liquidity perspective and harmful to existing and future investors in

[1] *Open-End Fund Liquidity Risk Management Programs and Swing Pricing; Form N-PORT Reporting,* 87 FR 77172 (Dec. 16, 2022), available at https://www.govinfo.gov/content/pkg/FR-2022-12-16/pdf/2022-24376.pdf (the "Proposing Release").
[2] On November 1, 2021, the sale of Wells Fargo Asset Management from Wells Fargo & Company to certain private funds of GTCR LLC and Reverence Capital Partners, L.P. closed, forming Allspring Global Investments, a privately held asset management firm with $465 billion in assets under management as of December 31, 2022. Included in Allspring Global Investments are Allspring Funds Management, LLC, and Allspring Funds Distributor, LLC, which serve as the investment manager and principal underwriter, respectively, to each of the Allspring Funds, and Allspring Global Investments, LLC, which serves as sub-adviser to most of the Allspring Funds.
[3] Assets under management in the Allspring Funds totaled approximately $226 billion as of December 31, 2022.

the funds.[4] We believe these counterintuitive results demonstrate that the proposed changes to LRM program parameters are irredeemably flawed, and we urge the Commission to engage with the industry outside the rulemaking process to determine whether and to what extent any such changes are warranted.

I. Liquidity in March 2020

At the outset, it is important to note that, given the statutory mandate to satisfy investor redemptions within seven days,[5] mutual funds have had robust LRM practices that long preceded the adoption and implementation of the specific program required by Rule 22e-4 (the "Rule"). We believe these pre-existing LRM practices remain vital components of any LRM program, as, in our experience, the model-dependent bucketing exercise required by the Rule has at times failed to illuminate liquidity issues identified through other means.

Indeed, this is exactly what we saw in March 2020, when global markets experienced significant and sudden stress and volatility caused by the onset of the COVID-19 pandemic. In our view, during this period equity markets provided ample liquidity due to surging volumes, but increased volatility made trading costs high and uncertain. On the other hand, fixed income markets, particularly in the high yield space, suffered from erratic liquidity. However, throughout this period, the vendor-supplied LRM model we use to implement the Rule's bucketing requirements continued to show a high degree of liquidity across our fund lineup. While we believed the model's assessment of liquidity was appropriate with respect to our equity funds, it did not match our investment teams' experience in some parts of the fixed income market. In particular, the model was not reacting quickly enough to changes in liquidity day-to-day and thus appeared to be overstating liquidity in high yield markets. As a result, we developed a systematic override framework which resulted in funds with high yield exposure seeing significant shifts out of the highly liquid bucket and into the other three liquidity buckets.[6]

Yet despite the turbulence in global markets, we assessed fund liquidity overall as remaining relatively robust during the period. While some fixed income funds saw their percentage of highly liquid assets drop significantly, the percentage of illiquid assets across all funds remained well below the 15% maximum throughout the period. This liquidity was necessary, as our funds, like others across the industry, experienced significant outflows, requiring them to sell assets to raise cash to meet redemption requests.[7] Although this elevated redemption activity led to increased concerns around liquidity, in particular with respect to fixed income funds, funds were able to meet redemption requests without exception.

In light of the period's nearly unprecedented short-term market stress, one might view this episode as a triumph of funds' LRM practices—but that is not the lesson the Commission draws. Instead, the

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[4] These results hold for larger emerging markets equity funds as well.
[5] Section 22(e) of the Investment Company Act of 1940.
[6] In the aftermath of this period, we worked with our vendor to review potential model enhancements and parameter specifications, recognizing the need to strike an appropriate balance between incorporating volatile model inputs and over-smoothing results. However, given that models are by their nature imperfect, we believe retaining the ability to apply qualitative judgments (including asset class-based considerations) is vital to assessing liquidity risk.
[7] As the SEC notes, "relatively few funds made use of borrowing to meet redemptions." Proposing Release at 77183.

Commission suggests that "some…funds were not prepared for the sudden market stress"[8] and that the "liquidity risk management program features of some funds adjusted slowly, making them less effective during the stress period for managing liquidity risk."[9] As a remedy for these alleged deficiencies, and in an effort to create "more objective and comparable liquidity classifications across funds,"[10] the Commission proposes to require changes to the Rule that would require funds to assume the existence of a uniform set of stressed conditions at levels that have never before existed, and to assume those never-before-seen conditions exist at all times for all funds regardless of a fund's individual characteristics. As discussed in detail below, the cumulative impact of the Proposal would lead to counterintuitive results, which suggests the Commission should, in consultation with the industry, reevaluate the Proposal in its entirety.

II. The Cumulative Impact of the Proposal

The Proposal would change numerous aspects of the Rule, which was adopted in 2016 and fully implemented in 2019. Among other things, the Proposal would:

- replace the Rule's fund-specific "reasonably anticipated trade size" ("RATS") with a uniform 10% "stressed trade size" ("STS") applied across each portfolio investment;
- require funds to adhere to prescriptive value impact standards;[11]
- change the day counting method from "T+1" to "T";[12] and
- remove the "less liquid" classification bucket.[13]

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[8] *Id.* The Proposing Release references efforts by funds to pursue emergency relief during this period to address potential liquidity concerns, some of which was granted, but none of which to our knowledge was utilized. *Id.* at 77182. In our view, prudent consultation with regulators in times of stress is something to be encouraged, and thus we are concerned that the Commission's citation of these discussions as a reason for significant regulatory changes may ultimately prove counterproductive.
[9] *Id*. at 77183. As acknowledged earlier, our vendor-supplied LRM model did in fact adjust slowly to market conditions in March 2020. However, it is important to note that model-dependent bucketing is only one aspect of our or any other industry-standard LRM program.
[10] *Id.* at 77184.
[11] Under the current Rule, the value impact standard (i.e., the phrase "significantly changing the market value of an investment") is not defined. The Proposal would define the value impact standard to mean (a) for exchange-traded instruments, any sale or disposition of more than 20% of average daily trading volume of such instruments, as measured over the preceding 20 business days (referred to herein as the "20% ADTV value impact standard"), and (b) for any other investment, any sale or disposition that the fund reasonably expects would result in a decrease in sale price of more than 1% (referred to herein as the "100 bps value impact standard").
[12] Currently, Allspring does not count the day on which a liquidity classification is made when determining the period in which an investment is reasonably expected to be convertible to cash (referred to herein as the "T+1 day counting method"), which we understand is the standard industry approach. The Proposal would require funds to count the day on which a liquidity classification is made when determining the period in which an investment is reasonably expected to be convertible to U.S. dollars (referred to herein as the "T day counting method"). We note that the proposed T day counting method does not align with the method used to meet investor redemption requests within the statutorily required seven days—for that purpose, funds and their service providers begin the day count the day after a redemption request has been received. This element of the Proposal thus becomes unmoored from the statutory requirement to meet redemption requests within seven days, the stated source of the Commission's rulemaking authority.
[13] The Proposal would also (i) require funds to maintain at least 10% of their net assets in highly liquid investments and (ii) prohibit funds from making asset class-based liquidity classifications. With respect to the latter, as noted

For the reasons detailed by ICI and SIFMA AMG, each of these proposed changes to LRM program parameters is individually objectionable. As explained in greater detail below, however, the cumulative impact of these changes would threaten the very viability of certain types of funds that are known to be quite liquid.

In assessing the potential impact of the proposed changes to the LRM program parameters across our fund complex, we have observed that it would significantly impact larger, actively managed small cap and emerging markets equity funds, among others. While these funds operate in segments of the market that may be more expensive to trade and thus generally have elevated liquidity risk, these markets have proven sufficiently liquid to facilitate trading needed for these funds to meet redemption requests, even during periods of market stress. Despite this demonstrated history of successfully managing liquidity risk, these funds would experience drastic increases in their measured illiquidity as a result of the proposed changes, even under normal market conditions.

To demonstrate the impact of the proposed changes, we reviewed publicly available holdings of five actively managed small cap funds sponsored by different firms with assets ranging from $4 billion to $7 billion and approximately 90 to 120 holdings each. We analyzed each assuming a 3% RATS[14] and a 20% ADTV value impact standard, which we believe are relatively standard LRM program parameters for these types of funds. As reflected in Figure 1, under the Rule's current LRM program parameters, these funds are primarily highly liquid, and in each case their illiquid investments are minimal, which in our experience reflects the realities of the small cap market. However, when applying the proposed changes to the LRM program parameters in their entirety, the measured liquidity profiles of these funds change dramatically, leaving four of the five funds well over the Rule's 15% illiquid limit.

Figure 1. Estimated Liquidity Bucketing Percentages for Five Small Cap Equity Funds Under Current and Revised Rule

	Current Rule 20% ADTV value impact standard 3% RATS T+1 day counting method				Revised Rule 20% ADTV value impact standard 10% STS T day counting method		
	Highly Liquid	*Moderately Liquid*	*Less Liquid*	*Illiquid*	*Highly Liquid*	*Moderately Liquid*	*Illiquid*
Fund A	94.4%	5.6%	0.0%	0.0%	25.6%	41.4%	33.1%
Fund B	76.6%	21.2%	1.5%	0.7%	23.3%	32.9%	43.8%
Fund C	91.2%	6.8%	2.1%	0.0%	19.1%	45.3%	35.5%
Fund D	99.4%	0.6%	0.0%	0.0%	35.0%	54.5%	10.4%
Fund E	92.9%	5.9%	0.4%	0.8%	21.6%	49.5%	28.9%

Note: Data as of 9/30/2022

earlier, we relied on asset class-based bucketing in March 2020 when we judged our vendor-supplied LRM model to be providing inaccurate results with respect to high yield assets, and believe it is important to retain this ability going forward.

[14] Allspring's current RATS methodology utilizes a 3% minimum for all funds, making upward adjustments based on fund performance, shareholder concentration and historical flows. This 3% minimum is intended to be conservative, and we believe a lower RATS would be appropriate for many of our funds.

Each proposed change to the LRM program parameters has a compounding effect. As shown in Figure 2, if the current parameters are adjusted only by adopting the SEC's proposed T day counting method, Fund C's highly liquid assets decrease significantly. If in addition the 3% RATS is replaced with the proposed 10% STS, Fund C's illiquid assets increase to 11.4%, nearing the Rule's 15% limit. Finally, the proposed elimination of the less liquid bucket requires moving less liquid assets to the illiquid bucket, increasing Fund C's illiquid assets to 35.5%, well above the regulatory limit.

Figure 2. Estimated Liquidity Bucketing Percentages for Fund C Under Various LRM Program Parameters

LRM Program Parameters	*Highly Liquid*	*Moderately Liquid*	*Less Liquid*	*Illiquid*	*Less Liquid + Illiquid**
20% ADTV value impact standard T+1 day counting method 3% RATS	91.2	6.8	2.1	0.0	2.1
20% ADTV value impact standard *T day counting method* 3% RATS	68.1	28.7	3.2	0.0	3.2
20% ADTV value impact standard T day counting method *10% STS*	19.1	45.3	24.1	11.4	35.5
50 bps value impact standard T day counting method 10% STS	34.4	46.4	12.1	7.2	19.3
100 bps value impact standard T day counting method 10% STS	93.8	4.2	2.1	0.0	2.1

Note: Data as of 9/30/2022. Each italics represents an incremental change to LRM program parameters.

* Reflects proposed elimination of the less liquid bucket, which would force those assets into the illiquid bucket.

These liquidity bucketing percentages are extremely sensitive to the required inputs. With respect to the value impact standard, we believe it may at times be appropriate for a fund to apply standards to small cap equity securities different from those required by the Proposal. Indeed, although historically we have predominantly used the 20% ADTV value impact standard for our equity funds, we evaluate multiple metrics when assessing our funds' overall liquidity risk and believe this flexibility is important, especially during periods of stress. With the proposed 10% STS, larger funds that invest in small cap or emerging market equity securities may need additional time to sell securities if strictly limited to 20% ADTV per day, resulting in the high levels of measured illiquidity shown above. If, however, instead of strictly limiting volume, a reasonable cost constraint of 50 or 100 bps is utilized, a fund's measured illiquidity may be very low. For example, as shown in Figure 2, although Fund C's illiquid assets exceed the regulatory limit under the Proposal's mandated 20% ADTV value impact standard, Fund C falls well below the illiquid limit when utilizing a reasonable price impact of 50 or 100 bps (although the elimination of the less liquid bucket would push the fund past the illiquid limit using the former). These significant differences in liquidity results suggest that, while these funds have some liquidity risk to manage, their holdings are not inherently illiquid.

Liquidity bucketing percentages are also sensitive to a fund's asset levels. Figure 3 shows how Fund C's liquidity bucketing percentages would change across different asset levels, assuming no change in its portfolio weightings. Mathematically, the 10% STS and the 20% ADTV value impact standard work together to penalize larger funds: as assets increase, trade size necessarily increases as a percentage of daily volume for each holding. However, we believe for two funds that differ only in their asset levels, the larger fund is generally less vulnerable to liquidity risk. When looking at actual historical flows, we tend to see larger funds having lesser day-to-day net outflows than smaller funds, even in times of market stress. This is likely driven by larger funds having more diversified shareholder bases and more established track records. Although smaller funds may have an easier time passing liquidity classification tests, they may be more vulnerable to large shareholder redemptions and larger daily flows as a percentage of assets.

Figure 3. Estimated Liquidity Bucketing Percentages for Fund C at Various Asset Levels

	Revised Rule		
	20% ADTV value impact standard T day counting method 10% STS		
Asset Levels	*Highly Liquid* %	*Moderately Liquid* %	*Illiquid* %
$500 million	96.9	3.1	0.0
$1 billion	90.5	9.5	0.0
$2 billion	63.7	31.5	4.7
$3 billion	53.5	37.0	9.4

Note: Data as of 9/30/2022

The cumulative impact of the proposed changes to LRM program parameters leads to results that defy common sense. Although we acknowledge that small cap and emerging market equity funds generally have elevated liquidity risk as compared to domestic large cap equity funds, the Proposal would require funds that have managed that risk effectively through multiple periods of severe market stress to fundamentally restructure their portfolios and/or reduce their sizes to comply with a set of parameters based on stressed conditions that have never and almost certainly will never exist.

III. Conclusion

We strongly object to the Proposal's proposed changes to LRM program requirements. While prescribing specific LRM program parameters may increase the comparability of liquidity classification across funds,[15] it comes at the cost of upending LRM programs that have proven effective during a time of

[15] Even with the proposed standardized LRM program parameters, bucketing results will still not be directly comparable given the differences in models employed by funds. For example, some liquidity models include trading volume on secondary or additional markets where securities trade while others do not. In addition, some liquidity models use a probabilistic approach, using varying degrees of statistical confidence levels when reporting results.

extraordinary stress. But the largest and most important costs will be borne by investors—to comply with the Proposal's artificial and arbitrary liquidity constraints, funds would be required to make fundamental changes to their portfolios, which would inevitably reduce investor returns, and/or be compelled to constrain their sizes, which would cause expense ratios to rise. We urge the Commission to exercise caution, to abandon this rulemaking and to engage with the industry to determine whether and to what extent changes to LRM program requirements are truly warranted.

We appreciate the opportunity to provide comments on the Proposal and welcome further engagement on any aspect of this letter.

Very truly yours,

Andrew Owen
President
Allspring Funds Management, LLC

Given this lack of direct comparability, the proposed public disclosure of liquidity bucketing results on Form N-PORT is likely to lead to investor confusion, and we therefore urge the Commission to retain the current approach.