February 14, 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 Reporting—Comments on Proposal [(File No. S7-26-22)]**

Dear Ms. Countryman:

The Independent Trustees and Directors (the "Boards") of the Lord Abbett Family of Funds (the "Funds") appreciate the opportunity to provide comments to the United States Securities and Exchange Commission (the "Commission") on the Commission's proposals to revise the liquidity risk management rules applicable to open-end funds and to require swing pricing by open-end funds (the "Proposals").[1] This letter discusses the Boards' significant concerns with the Proposals, which we are writing as representatives of the Funds and their shareholders.

The Lord Abbett Funds consist of 12 registered open-end investment companies, comprising 60 series, and three registered closed-end interval funds. The Lord Abbett Funds include a wide array of fixed-income, equity and funds of funds, including funds first launched in the 1930s, predating the Investment Company Act of 1940 (the "1940 Act"). As of December 31, 2022, the Lord Abbett Funds had approximately $147 billion in assets under management.

As Independent Trustees and Directors, we occupy a unique position relative to other industry participants. In the words of former Commission Chairman Arthur Levitt, we are "watchdogs" for fund shareholders, representing their interests independent of the concerns of management.[2] Although the Boards recognize the Commission's goals of better preparing funds for possible future stressed conditions and addressing concerns of potential shareholder dilution, we are concerned that the negative impacts of the Proposals to funds and their shareholders will outweigh any benefits.

We are aware that the Independent Directors Council (the "IDC") will be submitting a comment letter and of the concerns that will be expressed in the IDC's letter. We agree with those concerns and are submitting the following additional comments on the Proposals.

[1] Open-End Fund Liquidity Risk Management Programs and Swing Pricing; Form N-PORT Reporting, Securities Act Release No. 11,130, Investment Company Act Release No. 34,746, 87 Fed. Reg. 77,172 (proposed Dec. 16, 2022) (the "Proposing Release").
[2] Speech by Chairman Levitt (February 23, 1999), quoting Burks v. Lasker, 441 U.S. 471, 484 (1979).

**Summary**

We have the following concerns, which we discuss in more detail below.

- The Commission offers limited data justifying either of the Proposals. We strongly recommend that the Commission undertake a more extensive analysis of the current regulatory framework, justify the need for change and identify and target proposed changes based on the results of such analysis.
- The Proposals would disadvantage shareholders investing through intermediaries relative to shareholders investing directly, and may also result in retail shareholders being disadvantaged relative to institutional shareholders.
- The Proposals would disadvantage smaller/retail shareholders that are redeeming the same day as large investors.
- The Proposals may result in a shift away from mutual funds to less regulated products.
- The Proposals will potentially eliminate open-end bank loan funds as investment options for retail shareholders.

**Discussion**

**Lack of Data from the Commission Justifying the Proposals:** The Proposing Release states that the proposed amendments to Rule 22c-1 are intended "to mitigate dilution" of shareholders' interests."[3] However, the Commission provides no hard data to substantiate its claim that shareholder dilution is a serious problem which necessitates mandatory swing pricing. In fact, the Commission acknowledges that it cannot quantify many of the anticipated costs and benefits associated with the proposed swing pricing framework.[4]

Although the Proposing Release discusses the potential effectiveness of swing pricing as an anti-dilution mechanism, it also admits that in the time since the adoption of amended Rule 22c-1 (permitting but not requiring swing pricing), not a single U.S. fund has implemented swing pricing. We believe this is because of market structure concerns making the adoption of swing pricing extremely difficult and also because of the effectiveness of the liquidity management tools that funds and their advisers currently use to manage liquidity risk. These include the ability to redeem in kind, maintaining open communications with financial intermediaries and other investors to help manage large redemptions, interfund lending arrangements, committed bank lending facilities, accelerated settlement of portfolio trades in certain circumstances, and prudent portfolio and risk management which takes into account expected cash needs based on a fund's portfolio, shareholder base, and historical shareholder flow experience, as well as market conditions.

Similarly, the Proposals include significant amendments to Rule 22e-4 under the 1940 Act (the "Liquidity Rule") which would make the Liquidity Rule more prescriptive, including (but not

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[3] Proposing Release at 77,172.

[4] *See Id.* at 77,236 ("many of the benefits and costs discussed below are difficult to quantify") and 77,256 ("We are not able to quantify many of the costs associated with the proposed swing pricing framework for several reasons.") The Commission makes a similar statement acknowledging its inability to quantify the costs associated with its proposed changes to funds' liquidity risk management frameworks. *See Id.* at 77,250.

limited to) requiring all funds to maintain a 10% highly liquid investment minimum, removing the less liquid investment category and thereby expanding the definition of illiquid investments, and requiring funds to assume a 10% "stressed trade size" when making liquidity classifications. We are concerned with the significant and prescriptive revisions proposed to a rule that has only fully been in effect for less than four years and has served its purpose well. The Commission does not provide data indicating that the Liquidity Rule is not already effectively protecting shareholders by regulating funds' liquidity risks or cite to any real shortcomings with the current rule.

Before so significantly changing the framework under which investors buy and sell mutual fund shares, the Commission should undertake a more extensive economic analysis of the impact of requiring across-the-board swing pricing and implementing the proposed changes to the Liquidity Rule and whether the benefits outweigh the significant costs and potential harms to investors, including harms arising from effectively forcing funds to invest in lower returning investments to comply with the Proposals. We suggest that the Commission issue a concept release, solicit industry feedback through industry roundtables and outreach, and draft any resulting rules to target any empirically supported shortcomings of the current regulatory regime that are identified through that process.

**Shareholders Investing through Intermediaries Will Be Disadvantaged Relative to Shareholders Investing Directly:** Mutual fund shareholders expect that orders placed before 4:00 p.m. (whether directly to the fund or through an intermediary) will receive that day's price. In recognition of the challenges faced by intermediaries to sort and transmit investors' orders and to allow shareholders to place orders through these intermediaries up to the same 4:00 p.m. cut-off time afforded to direct investors, the Commission permitted intermediaries to forward orders to mutual funds after the 4:00 p.m. close.[5] The Commission now seeks to upend this expectation, as a result eliminating the level playing field it had previously established.

Currently, over 80% of mutual fund shareholders hold mutual fund shares indirectly through intermediaries such as brokers and advisory accounts or through retirement plans.[6] With respect to the Lord Abbett Funds, approximately 99% of the assets are held through such financial intermediaries. These intermediaries often allow shareholders to hold mutual fund shares in multiple fund families and to make exchanges across fund families on a same-day basis. We believe shareholders will be harmed if they are forced to choose between using an intermediary and having until 4:00 p.m. to submit their orders.

Specifically, if a hard close were adopted, shareholders holding mutual fund shares through intermediaries would be disadvantaged relative to direct investors. Intermediaries would likely have to establish earlier cut-off times for their retail customer trades so that they can batch and submit their trades to the mutual fund families by 4:00 p.m. Shareholders transacting through intermediaries would not be able to benefit from late-breaking market information (arising after

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[5] *See* Staff Interpretive Position 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).

[6] *See* Inv. Co. Inst., 2022 Investment Company Fact Book 124 (2022), https://www.icifactbook.org/. A small percentage of mutual fund investors hold assets directly with fund families, which allows them to place trades up to 4:00 p.m. The hard close is not likely to impact their ability to place trades up until the close of the market unless fund families establish earlier cut-offs to aggregate direct retail trades.

the cut-off but before 4:00 p.m.). On the other hand, shareholders who can buy directly from the funds and can wait to place their orders until immediately before 4:00 p.m. will have the benefit of whatever information becomes available after intermediary investors have had to place their orders for the day. This disparity is exacerbated for shareholders physically located on the west coast, such as investors in the Lord Abbett California Tax-Free Income Fund, who would have to place their orders very early in their trading day. Furthermore, we are concerned that different intermediaries would impose different cut-off times for investors based on their own ability to process and transmit data to the mutual funds by 4:00 p.m. This may result in shareholders having to keep track of different order cut-off times if investing through multiple intermediaries (for example, through both an advisory account and a retirement plan).

We are also concerned that institutional investors will be more easily able to structure their fund ownership as direct investments (less impacted by the hard close) or to invest through collective investment trusts or separate accounts (not subject to the Proposals at all), potentially leading to disparate treatment between institutional and retail shareholders.

*Taken together, these changes contradict a fundamental premise of the 1940 Act—"that fund shareholders be treated equitably when buying and selling their fund shares."*[7]

**Smaller/Retail Investors Could be Disadvantaged by a "Swung Down" NAV:** The Proposals will require that a fund's current NAV be adjusted by a swing factor on any day that the fund has net redemptions. When a fund has net redemptions, the NAV will be "swung down" such that redeeming shareholders will receive a price lower than NAV for their shares. For example, if the swing results from a redemption by a large investor, *smaller investors who are unfortunate enough to be redeeming the same day (in amounts that do not raise issues of shareholder dilution or the other concerns described in the Proposals) would have their redemption proceeds reduced.*

In addition, purchasing shareholders will pay a lower price for shares at the "swung down" price as compared to the current NAV. The Commission has argued that the operation of these swung prices will reduce the potential for dilution of shareholders who are not currently transacting in the fund's shares. The Commission does not acknowledge, however, that allowing purchases to buy shares of a fund at a price lower than NAV could also *disadvantage long-term shareholders by, in effect, creating a discount for only certain purchasers*. A similar problem arises in a net subscription scenario: when net purchases exceed 2% of a fund's net assets, the current NAV will be "swung up" (*i.e.,* increased). Because the same swung price is applied on a given day to both purchasing and redeeming shareholders, shareholders that redeem on a day where the NAV is swung up will receive a price higher than current NAV, *unfairly favoring those shareholders to the detriment of those shareholders who remain in the fund*.

**The Proposals Could Drive Investors to More Lightly Regulated Vehicles:** Although the Commission appears to assume that retirement plans and intermediaries would change their systems to accommodate the Proposals, we are concerned the likely outcome for many investors would be the *replacement* in retirement plans and intermediary platforms of mutual funds with other investment vehicles that do not necessitate these system changes, such as CITs and separate

[7] Open-End Fund Liquidity Risk Management Programs; Swing Pricing; Re-Opening of Comment Period for Investment Company Reporting Modernization Release, 80 Fed. Reg. 62,274, 62,275 n.2 (Oct. 15, 2015).

accounts. These products *do not include the protections of the 1940 Act*, including the requirement of an independent board, that have served investors for over 80 years. We believe it could not have been the Commission's intent that, in an effort to protect investors, the Commission would propose rules that might have the opposite effect.

**Potential Elimination of Certain Types of Funds:** The Proposals would remove the Liquidity Rule's "less liquid" investment category and expand the "illiquid" investments category to include investments that are currently classified as less liquid. We are concerned that this change will make open-end bank-loan funds, including the Lord Abbett Floating Rate Fund, unviable.

The Commission states that the proposed changes will "help prepare funds for future stressed conditions by reducing the risk of a fund not being able to meet shareholder redemptions."[8] Currently 90% of bank loans are reported by funds as less liquid in N-PORT filings; [9] under the Proposals, these would likely be classified as illiquid. As a result, open-end funds with 15% or more of their assets in bank loans or other less liquid investments would be required to change their strategy, liquidate, or convert to a closed-end fund structure notwithstanding the expectations of investors, supported by years of experience, that they would be able to invest in the bank loan asset class through an open-end mutual fund. The Commission does not cite to any period in history when open-end bank loan funds had trouble meeting redemption requests and even recognizes that bank loan funds "were able to meet redemption requests during March 2020, a period of significant outflows."[10] We believe that removing open-end bank loan funds, and potentially other types of funds, as investment options for shareholders is an extreme solution to a potential *future harm that eliminates shareholder choice, at least for smaller or retail shareholders who are unable to invest in the bank loan asset class through private funds or separate accounts*. To the extent that the Commission has concerns with bank loan funds, we believe it should consider more targeted approaches that allow them to remain available to investors while addressing the Commission's specific concerns.[11]

**<u>Conclusion</u>**

The Boards strongly believe that the Proposals must be considered in light of their effects on mutual fund shareholders with clear justification based on actual data. We also ask that the Commission consider the necessity of the Proposals generally in light of the effectiveness of the current Liquidity Rule and funds' existing liquidity risk management programs. A full understanding of the implications of the Proposals will only be appreciated through widespread engagement with mutual fund industry participants, including boards of trustees. We therefore urge the Commission to convene working groups of relevant industry participants to consider the feasibility and implications of swing pricing and the hard close requirement, as well as alternative anti-dilution measures.

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[8] *See* Proposing Release at 77,190.
[9] *Id*. at 77,191.
[10] *Id.*
[11] We believe that similar considerations could apply to other types of funds, such multisector funds, local emerging market debt funds, mortgage-backed securities funds that allocate to early buyouts, and high yield funds that allocate to bank loans.

The Boards are grateful for the opportunity to comment on the Proposals.

Sincerely,

/s/ James L.L. Tullis
James L.L. Tullis, Independent Chair, Lord Abbett Funds

On behalf of:

Evelyn E. Guernsey
Julie A. Hill
Kathleen M. Lutito
James M. McTaggart
Charles O. Prince
Karla M. Rabusch
Lorin Patrick Taylor Radtke
Leah Song Richardson
Mark A. Schmid

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