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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 Rule Proposals [(File No. S7-26-22)]**

Dear Ms. Countryman:

The Board of Trustees of the J.P. Morgan Funds (the "Board") appreciates the opportunity to provide comments to the United States Securities and Exchange Commission (the "Commission" or "SEC") on the Commission's proposals to revise the liquidity risk management requirements applicable to open-end funds and to require swing pricing by open-end funds except for certain excluded funds (the "Proposals").[1] This letter discusses the Board's significant concerns with the Proposals.

The J.P. Morgan Funds consists of 9 registered open-end investment companies advised by J.P. Morgan Investment Management Inc. ("JPMIM"). The J.P. Morgan Funds Complex includes mutual funds, money market funds and exchange-traded funds investing over a broad array of asset classes and strategies. As of January 31, 2023, JPMIM offered 153 mutual funds and ETFs with a total of approximately $520.2 billion in assets under management (excluding money market funds).

Independent trustees occupy a unique position relative to other industry participants. In the words of former Commission Chairman Arthur Levitt, independent trustees are "watchdogs" for fund shareholders, representing their interests independent of the concerns of management.[2] As Trustees and Directors, our responsibility is to represent and act in the best interests of the funds' shareholders. Although the Board recognizes the Commission's goals of better preparing funds for possible future stressed conditions and addressing concerns of potential dilution associated

[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 (December 16, 2022) (the "Proposing Release").
[2] Speech by Chairman Levitt (February 23, 1999), quoting Burks v. Lasker, 441 U.S. 471, 484 (1979).

with investor transactions, we are concerned that the potential negative impacts of the Proposals to funds and their shareholders will outweigh any benefits. Although we have never submitted a comment letter on a rule proposal, we feel so strongly that we are compelled to weigh in.

We understand that the Independent Directors Council (the "IDC") is submitting a comment letter on the Proposals and are aware of the comments that will be raised in that letter. We endorse those comments and would like to submit the following additional comments on the Proposals.

Comments on Swing Pricing Proposals

- **Justifying Swing Pricing by Reference to the European Model is Misplaced:** The Commission cites to the use of swing pricing in Europe for its support of mandating swing pricing for all open-end funds except certain excluded funds. The Board acknowledges that European funds, including funds sponsored by JPMIM affiliates, have implemented swing pricing and that a properly constructed swing pricing regime can benefit investors. However, there are several critical differences between European markets and U.S. markets that we believe would make swing pricing, at least as currently proposed, unworkable in the U.S. In addition to significant differences in market structure between the U.S. and European markets, the European swing pricing model is permissive and allows for significant flexibility in deciding whether to adopt and how to implement swing pricing. In Europe swing pricing is one of several liquidity risk management tools that may be used by funds; it is not mandated. In addition, unlike the proposed prescriptive mandatory model put forth by the Commission, the European swing pricing model is flexible; for example, it does not require funds to include market impact in swing factors and European funds can take into consideration fund-specific factors when setting swing thresholds.

- **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 order 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 permits intermediaries to forward orders to mutual funds after the 4:00 p.m. close, honoring the time the order was placed with the intermediary.[3] 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.[4] These intermediaries often allow investors 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.

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[3] *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).

[4] *See* Inv. Co. Inst., 2022 Investment Company Fact Book 124 (2022), https://www.icifactbook.org/. A relatively 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.

to submit their orders. In addition, we are concerned that retirement plan shareholders will not even have this choice as they may be required to comply with the deadline imposed by their retirement plan administrator.

Specifically, if a hard close were adopted, intermediaries would likely have to establish earlier cut-off times for their retail customer trades so that the intermediaries could batch and submit their trades to the mutual fund families by 4:00 p.m. This would raise a number of issues that could adversely affect shareholders. For example, shareholders investing through intermediaries would not be able to benefit from market information that becomes available later in the day (arising after the cut-off but before 4:00 p.m.). By contrast, shareholders who can buy directly from the funds and can wait to place their orders until closer to 4:00 p.m. can benefit from information that 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, who likely would have to place their orders very early in their day.

We are also concerned that institutional investors will be better able to structure their fund ownership as direct investments (less impacted by the hard close) or to invest through collective investment trusts ("CITs") or separate accounts (not subject to the hard close), potentially leading to disparate opportunities for 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."[5] If the hard close requirement is adopted, shareholders transacting through intermediaries will be forced to make transaction decisions hours before their direct shareholder counterparts.

- **Smaller/Retail Investors Could be Disadvantaged by a "Swung" NAV:** The Proposals would 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 Proposing Release) would have their redemption proceeds reduced. A similar issue 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, potentially favoring those investors as compared to investors who happen to redeem on a different day.

  Although we understand that long-term shareholders may benefit from a thoughtfully constructed swing pricing program, we are concerned that the Proposals, which would impose a prescriptive swing pricing regime with limited flexibility to use other dilution management tools, would not provide funds with the flexibility to address and/or mitigate issues like those identified above.

[5]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).

- **The Proposals May 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 that the outcome for many investors would be the replacement in retirement plans and intermediary platforms of mutual funds with other investment options that do not necessitate costly system changes, such as CITs and separate accounts. Such products do not include the protections of the 1940 Act, including the requirement for independent boards, which 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 may in fact reduce protections for many investors.

Comments on the Liquidity Rule Proposals

- **The Proposals Do Not Take into Account Differences among Funds:** If the Commission believes further regulatory action is needed, we believe a principles-based approach, rather than a prescriptive, one-size-fits-all rule, would be better. A principles-based approach would allow liquidity risk management programs and tools that are tailored to the characteristics of each fund. Funds vary widely in size, shareholder characteristics, asset classes, investment strategy, portfolio composition and portfolio structure. A liquidity risk management approach tailored to the characteristics and circumstances of each fund is likely to be more effective than an inflexible, uniform approach.

  Two examples of what we believe are unnecessarily prescriptive approaches are the universal 10% highly liquid investment minimum ("HLIM") and the stressed trade size ("STS") of 10% of each portfolio investment, which would replace the fund-specific reasonably anticipated trade size ("RATS"). Notwithstanding these two 10% standards, the Commission itself finds that outflows of 10% in a given week are rare.[6] As the Commission acknowledges, shareholders may be harmed by these standards as funds may need to alter the composition of their portfolios in order to comply, which could negatively affect fund performance by forcing funds to hold investments with lower returns.[7]

- **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. The Commission states that this 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; under the Proposals,[9] 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

[6] *See* Proposing Release at 77,187 (stating that "an analysis of weekly flows of equity and fixed-income funds over a period of more than ten years, outflows greater than 6.6% occurred 1% of the time in a pooled sample across weeks and funds. Based on this analysis, we estimate that a random fund in a random week has approximately a 0.5% chance of experiencing redemptions in excess of the 10% stressed trade size, and there were 3.4% of weeks where more than 1% of funds experienced net redemptions exceeding the proposed stressed trade size.") (internal citations omitted)
[7] *Id*. at 77,251.
[8] *See* Proposing Release at 77,190.
[9] *Id*. at 77,191.

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] 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.

* * *

We recognize that the Commission is grappling with difficult issues while seeking to protect investors. However, before so significantly changing the framework under which investors buy and sell mutual fund shares and investment advisers manage fund portfolios, we believe the Commission should undertake a more extensive and rigorous 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 funds and investors. We suggest that the Commission issue a concept release, convene industry and investor roundtables and working groups, solicit feedback over a reasonable period of time, and draft any resulting rules to target any specific identified supported shortcomings of the current regulatory regime that are identified through that process.

[10] *Id.*

The Board is grateful for the opportunity to comment on the proposed rules. If you have any questions or would like to discuss anything in this letter further, we welcome the opportunity to engage with you. Please feel free to contact myself or counsel to the Independent Trustees, Bryan Chegwidden, Michael Doherty or Elizabeth Reza at Ropes & Gray LLP.

Sincerely,

/s/ John F. Finn
John F. Finn
Chairman of the Board of Trustees

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