J.P.Morgan
Asset Management

George C.W. Gatch
Chief Executive Officer

July 6, 2023

Vanessa Countryman
Secretary
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 (File No. S7-26-22)

Dear Ms. Countryman:

This letter supplements our February 14 comment letter on the above-referenced file.[1] In that letter, we made the following recommendations, among others:

- The Commission should retain the existing definition of reasonably anticipated trade size ("RATS") across funds. To the extent the Commission is concerned about a lack of specific parameters, it may choose to provide further guidance on how funds consider stress in determining a "reasonably anticipated" trade size.[2]
- The Commission should maintain the "primarily" exclusion to the highly liquid investment minimum (HLIM) requirement, and provide further guidance on how funds in scope for this requirement should set an HLIM.[3]
- When calculating market impact for shares listed on a national securities exchange or a foreign exchange, the Commission should permit funds to determine lookback periods based on a documented governance process.[4]

In this letter, we offer further detail on these recommendations.

[1] Letter from George C.W. Gatch, CEO – Global Funds Management and Institutional, J.P. Morgan Asset Management to Vanessa Countryman, Secretary, Securities and Exchange Commission, dated February 14, 2023, available at https://www.sec.gov/comments/s7-26-22/s72622-20157314-325657.pdf ("Fund LRM letter").

[2] *Id.* at 3.

[3] *Id.* at 8.

[4] *Id.* at 5.

I. Further guidance on RATS

The proposed rule would require all funds to assume a "stressed trade size" of 10% of each investment when making liquidity classifications. The proposed changes are intended to address "variability in funds' reasonably anticipated trade sizes and the potential ineffectiveness of small trade sizes in helping a fund prepare for stress."[5] As our Fund LRM letter explained, JPMAM believes that the proposed uniform standard across funds is not appropriate, and the 10% requirement is too large for most funds. Our letter recommended that the SEC staff could instead provide further guidance on how a fund should consider stress in determining a "reasonably anticipated" trade size. We suggested that such guidance could include, for example, how each fund should consider factors such as its historical experience including extreme outflows, fund size, and investor concentration.[6] Below we offer additional detail on how these considerations could be implemented.

To assess historical flows, the staff could recommend that each fund should examine its largest outflows over consecutive days for a specified time period. We believe that cumulative net flows over three consecutive business days within the previous two years at the 95th percentile provides a sufficient indication of flows that a fund may experience in future stressed conditions. Should the staff take this approach, it would be appropriate to permit funds to exclude one-off redemptions if the redemption is not representative of a reasonably anticipated future event (e.g., a redemption in-kind, client asset reallocation). New funds that lack historical flows could use a flow history from a substantially similar fund or use a baseline estimate.

To assess investor concentration, the staff could recommend that each fund consider the share of the largest investors relative to the liquidity of the portfolio. We believe that the top two shareholders or the smallest number of investors that collectively hold 5% of AUM provides a sufficient indication of investor concentration.[7] If the size of the largest investors is greater than the amount of assets a fund can sell in a single day, the fund should consider factors that may raise redemption-based liquidity risks to the fund. These factors should include the underlying investor composition (e.g., whether the investor is a single decision maker or an omnibus account of advisers) and likelihood of an unexpected large flow.

This assessment of historical flows and investor concentration should be performed on a regular basis (e.g., monthly). The assessment and any revisions to a fund's RATS should be documented, including any manual adjustments or exclusions.

[5] *See* Proposing Release at 45.

[6] *See* Fund LRM letter at §I.a.1.

[7] In some cases, the largest shareholders of record will hold more than 5% but represent a collection of investors aggregated through an intermediary, platform, or other type of omnibus account.

II. Further guidance on the HLIM

The proposed rule would remove the primarily exclusion and require all funds to establish HLIM shortfall procedures. The proposal would also require all funds to adopt an HLIM of at least 10% of the fund's net assets. The proposed rule is intended to address the concern that funds currently relying on the primarily exclusion "do not have the benefit of shortfall procedures, including board oversight, to respond to events or market conditions that may cause the fund to fall under its previously determined level of primarily held highly liquid investments."[8] The proposed 10% HLIM minimum is intended to improve the ability of funds to meet shareholder redemptions in stressed scenarios and minimize any competitive advantage for similar funds.[9]

As our Fund LRM letter explained, JPMAM believes that the benefits associated with the proposed changes as applied to primarily highly liquid funds would not justify the associated burdens. Our letter recommended that the Commission retain the primarily exclusion, and provide further guidance on how funds in scope for this requirement should set an HLIM.[10] Below we offer additional detail on how these recommendations could be implemented.

The staff could provide guidance clarifying that to rely on the primarily exclusion, a fund should hold at least 50% of its net assets in highly liquid assets. The guidance could also recommend that to rely on the primarily exclusion, a fund should confirm on a regular basis (e.g., monthly) that it meets this threshold. A 50% highly liquid threshold would provide a buffer of highly liquid investments that is substantially larger than the proposed 10% minimum. Requiring primarily highly liquid funds to adopt shortfall procedures would necessitate a recurring resource cost that likely would not enhance fund liquidity risk management. For funds that do not qualify for the primarily exclusion, the staff could provide guidance on how a fund should set its HLIM. Such guidance could identify risk factors a fund should consider in setting its HLIM. The factors could include an assessment of historical flows and investor concentration aligned with the process to establish RATS as described in Section I above.

III. Governance process for determining lookback periods

The proposed rule would define "significant change in market value" for listed securities as a sale that is more than 20% of average trading volume over the preceding 20 business days. These changes are intended to provide "an appropriate measure of daily trading volume, which would reflect current market conditions as well as consider a period of recent market history."[11] As we explained in our Fund LRM letter, while we agree that a 20% volume threshold is appropriate, we believe the proposed 20-day lookback period is too short and will lead to a distorted picture of

---

[8] *See* Proposing Release at 81.

[9] Proposing Release at 81.

[10] *See* Fund LRM letter at §I.a.5.

[11] Proposing Release at 51.

trading conditions.[12] Our letter recommended that the SEC not prescribe a specific lookback, and instead permit funds to determine lookback periods based on a documented governance process. We offer additional detail below.

Historical trading volumes demonstrate that trading can increase in short bouts of stress, causing funds to appear more liquid if they rely on historical volumes to assess market depth. This effect is more pronounced with a shorter lookback period. For example, during the market stress surrounding March 2020, a period in which the S&P500 declined by about 34%, the average daily trading volume of US listed equities nearly doubled relative to the year prior.[13] As markets began to stabilize, market depth would have been 35% greater using a lookback of 20 days relative to 60 days.[14] The shorter lookback period would have made funds less likely to reclassify assets into less liquid buckets.

Instead of requiring a 20-day lookback period, the staff could provide guidance on how a fund should establish and maintain a process to determine significant changes in market value. The guidance could recommend that the liquidity risk officer should oversee the methodology to calculate significant changes in market value, including establishment of the lookback period. This determination should include a change control governance process with signoff by a senior risk officer. The liquidity risk officer should also include a report of any changes to the methodology in its update to the fund board on the effectiveness of the liquidity risk program.

* * *

JPMAM appreciates the opportunity to provide additional comments on the Commission's proposed rule. We would be pleased to provide any further information or respond to any questions that the Commission or the staff may have.

Very truly yours,

/s/ George C.W. Gatch

George C.W. Gatch

Cc: The Honorable Gary Gensler, Chair
The Honorable Hester M. Peirce, Commissioner
The Honorable Caroline A. Crenshaw, Commissioner

[12] *See* Fund LRM letter at §I.a.2.A.

[13] Average daily notional value traded on NASDAQ and NYSE from February 20, 2020 through March 23, 2020, relative to the same period the year prior. Source: Cboe Exchange, Inc., available at: https://www.cboe.com/us/equities/market_statistics/historical_market_volume/.

[14] *Id.*

The Honorable Mark T. Uyeda, Commissioner
The Honorable Jaime Lizárraga, Commissioner
William A. Birdthistle, Director, Division of Investment Management
Sarah ten Siethoff, Deputy Director, Division of Investment Management