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September 5, 2023

Submitted electronically through: https://www.sec.gov/rules/submitcomments.htm

Ms. Vanessa A. 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 Reporting: File Number S7-26-22

Dear Ms. Countryman,

Fidelity Investments ("Fidelity")[1] appreciates the opportunity to provide supplemental comments to the Securities and Exchange Commission ("SEC" or "Commission") on its proposed rule and form amendments relating to liquidity risk management programs and swing pricing (the "Proposal" or "Proposed Rule").[2]

As we stated in Fidelity's February 14, 2023 Comment Letter ("Fidelity Comment Letter"), we support Rule 22e-4 and its stated objective to promote effective liquidity risk management throughout the open-end investment company industry.[3] We believe that the Commission already has in place a workable rule that recognizes that different funds may have differing levels of liquidity and exposure to liquidity risk, and that funds should be allowed to tailor their liquidity risk management programs to their particular risks and circumstances.

Fidelity agrees with the Commission's desire to improve comparability and consistency across funds' liquidity risk management programs. However, as described in the Fidelity Comment Letter, we believe that replacing the current Rule 22e-4 principles-based approach with the Proposal's standardized, prescriptive approach will not produce more meaningful liquidity classification outcomes. On the contrary, we believe that the Proposal's prescriptive approach will misrepresent funds' liquidity profiles, adding unnecessary costs and diminishing fund returns, and ultimately **force the liquidation of open-end bank loan funds eliminating a highly valued investment option for retail investors.**

I. Executive Summary

[1] Fidelity is one of the world's largest providers of financial services, including investment management, retirement planning, portfolio guidance, brokerage, benefits outsourcing and many other financial products and services to approximately 40 million individuals and institutions, as well as through 13,500 financial intermediary firms. Fidelity submits this letter on behalf of Fidelity Management & Research Company LLC, the investment adviser to the Fidelity family of mutual funds.

[2] *See* Open-End Fund Liquidity Risk Management Programs and Swing Pricing; Form N-PORT Reporting, Release Nos. 33-11130; IC-34746, RIN 3235-AM98; File No. S7-26-22 (November 2, 2022) ("Proposing Release"), *available at* https://www.sec.gov/rules/proposed/2022/33-11130.pdf.

[3] *See* https://www.sec.gov/comments/s7-26-22/s72622-20157344-325691.pdf.

The comments made in this supplemental letter reiterate Fidelity's strong opposition to the SEC's proposed removal of the less liquid investment category from the liquidity classification framework and the treatment of those securities as illiquid investments. Most concerning is the highly detrimental impact to funds that primarily invest in bank loans and the consequences which will make dedicated open-end bank loan funds unworkable. In the remainder of our letter, we will discuss in detail the points summarized below.

1. ***Eliminating the less liquid investment category will deny retail investors a highly valued investment option***. Eliminating the less liquid investment category in the liquidity classification framework will cause the liquidation of bank loan funds, denying retail investors a longstanding and highly valued investment option.

2. ***Alternative fund structures fail*** to provide investors the same value as open-end bank loan funds. Retail investors overwhelmingly favor open-end bank loan funds and do not receive the same benefits from a closed-end fund structures, which are typically more expensive compared to open-end bank loan funds and trade at a discount to their net asset value ("NAV").

3. ***In the interest of preserving open-end bank loan funds, Fidelity recommends*** a 10% highly liquid investment minimum ("HLIM") for bank loan funds as a reasonable alternative to eliminating the less liquid investment category.

II. Proposed Elimination of the Less Liquid Investment Category is Unnecessary

A. Bank Loans Benefit the U.S. Economy

Bank loans are debt securities issued by companies or other entities with floating interest rates that reset periodically. Bank loans are often issued in connection with recapitalizations, acquisitions, leveraged buyouts, and refinancings and therefore provide a vital source of capital for small to mid-size businesses. These small to mid-size companies employ a significant number of Americans and serve as the primary growth engine for the U.S. economy. In addition, bank loans provide an important balance sheet management tool for companies because, unlike high yield bonds, they have limited call protection (typically six months) and are prepayable at par.

Open-End Bank Loan Funds are a Valued Investment Choice

Open-end bank loan funds offer a unique risk-return profile relative to other asset classes and can be an important element of portfolio diversification for retail mutual fund investors. Bank loan funds have historically benefited shareholders when central bank policy rates are rising, and other asset classes are underperforming. Furthermore, open-end bank loan funds provide a consistent source of investment return over time as illustrated by the loan market's positive return in 23 of the past 26 years.[4] During this period, a decline of more than 1% only

[4] *See* Morningstar LCD as of June 30, 2023.

occurred once (a 29% decline in 2008 during the great financial crisis) and was followed by a sharp rally of over 50% in 2009. As described in greater detail below, retail investors hold the largest share of the approximately $14 billion in assets held in Fidelity's open-end bank loan funds. The Proposed Rule will force the liquidation of open-end bank loan funds eliminating a highly valued investment option for retail investors. Retail investors will be forced to reassess their investment portfolio composition as they search to reallocate the bank loan portion of their portfolio into a compatible strategy. Beyond the portfolio disruption, retail investors may face other negative implications including unanticipated tax liabilities.

Should the Commission decide to eliminate the less liquid investment category and force the closure of open-end bank loan funds, investment companies may decide to launch other investment vehicles to address retail investor demand. However, investors overwhelmingly prefer open-end registered funds to other investment vehicles such as closed-end funds. The reasons behind this preference include expense and performance. Closed-end bank loan fund expense ratios and management fees can on average be two to three times higher than open-end bank loan funds. Also, closed-end bank loan funds typically trade at a discount to their NAV, negatively impacting investor return. Forcing retail investors seeking exposure to bank loans to redirect their investments to closed-end funds will diminish investor return without any offsetting benefit.

B. Bank Loan Fund Liquidity is Effectively Managed Through HLIMs and Other Readily Available Liquidity Sources

As stated in the Fidelity Comment Letter, we support current Rule 22e-4's requirement for funds that do not primarily hold highly liquid investments to determine and maintain an HLIM.[5] Due mainly to the extended settlement times required for bank loan investments, Fidelity's bank loan funds established and continue to maintain an HLIM. Consistent with the Rule and Fidelity's prudent portfolio management practices, these funds maintain a balance of cash, cash equivalents, and other highly liquid investments as readily available sources of liquidity to meet near-term shareholder demands. Since the adoption of current Rule 22e-4 and the imposition of the HLIM requirement for funds that do not primarily hold highly liquid investments, Fidelity's bank loan funds have consistently remained compliant with their respective HLIM levels and have successfully met shareholder redemptions, even during times of market volatility.

Other Liquidity Sources

During times of unexpectedly high shareholder redemptions, bank loan funds have other means of accessing liquidity in addition to their HLIM. Fidelity's bank loan funds have established liquidity sources, which include borrowing arrangements made via an interfund lending facility, and both committed and non-committed lines of credit. These additional liquidity sources can be used to manage and access liquidity especially during times of market volatility helping to bridge the timing between bank loan sale and settlement, making the proposed amendments unnecessary and harmful to investors.

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[5] Rule 22e-4(b)(1)(iii).

III. The Proposal Will Eliminate Open-End Bank Loan Funds

A. Sweeping Amendments to Rule 22e-4 Render Bank Loan Funds Unworkable

The proposed amendments to replace the current Rule 22e-4 principles-based approach with a standardized, prescriptive approach will not produce more meaningful outcomes for fund shareholders and will misrepresent funds' liquidity profiles, add unnecessary costs, limit investor choice, and diminish fund returns to the detriment of fund shareholders.

No example of this outcome is clearer than the extreme impact the Proposal will have on open-end bank loan funds and their investor. The proposed elimination of the less liquid investment category from the current liquidity risk management categorization framework, coupled with the proposed 15% limit on illiquid investments, will make it impossible for open-end bank loan funds to remain viable. Based on a recent analysis, Fidelity estimates that eliminating the less liquid investment category will cause each of Fidelity's open-end bank loan funds' portfolios to hold illiquid investments in excess of 85% of their respective total net assets, drastically exceeding the 15% limitation. As a result, these bank loan funds will no longer be viable in their current open-end structure, and they will need to be liquidated. We believe this will be the result for all other open-end bank loan funds currently offered.

Furthermore, we do not believe that a closed-end fund or other alternative fund structure, such as a collective investment trust ("CIT") or private fund, is suitable, preferable, or in some cases accessible to most existing shareholders. The forced closure of these funds will reduce overall investor choice by eliminating investors' ability to access a highly desirable asset class. Further, retail investors who own open-end bank loan funds may not be fully aware of the Proposal's impact. It is a foreseeable consequence that these investors will not know of a fund's forced liquidation, while more sophisticated investors, such as advisors, will understand the impact and will therefore sell their holdings prior to any fund liquidation. Thus, leaving remaining retail investors in the fund with the exact problem the Proposal is purportedly trying to solve.

B. Consequences are Fatal to Open-End Bank Loan Funds

Fidelity has managed open-end bank loan funds for over 20 years with a proven record of meeting shareholder redemptions through several challenging market cycles. As one of the largest asset managers in the industry, Fidelity continuously strives for the best outcome for our customers. We manage the largest open-end bank loan fund, which has over $11 billion in total net assets. Our Fidelity Advisor Floating Rate High Income Fund ("Fund") has over 119,000 household investors.[6] These direct retail investors rely on this Fund to provide exposure to an asset class they would not otherwise have access to within their diversified portfolios. This Fund is also held in over 1,800 plan sponsor fund lineups, in both 403(b) plans and 401(k) plans.[7] For these investors, the Fund represents an important portion of a retirement portfolio that provides

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[6] *See* Fidelity Advisor Floating Rate High Income Fund as of March 31, 2023.

[7] *See* Fidelity Advisor Floating Rate High Income Fund as of March 31, 2023.

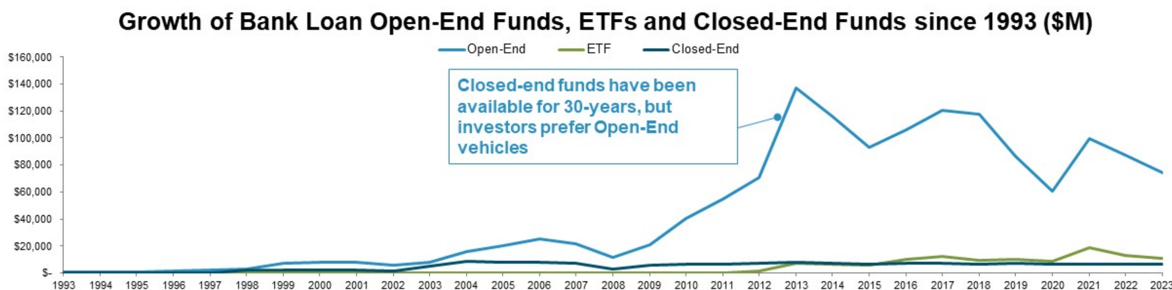
stable performance to help ensure a secure retirement. The proposed amendments to Rule 22e-4 will mean the shuttering of this Fund and every other open-end bank loan fund, effectively removing this asset class from investor portfolios and limiting investor choice.

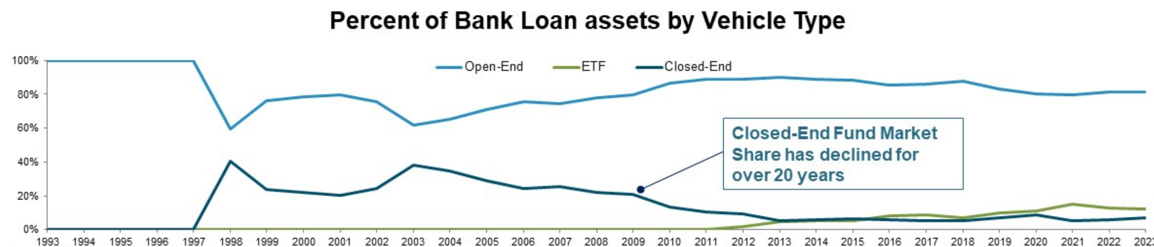
C. Alternative Fund Structures Limit Shareholder Returns and are More Expensive

If the Proposal is adopted in its current form, which will result in the elimination of open-end bank loan funds, investment companies will be faced with a decision. Decline to restructure their open-end bank loan funds, thus eliminating those funds and reducing competition and choice for investors, or restructure into closed-end bank loan funds, CITs or private funds, to allow fund investors the opportunity to continue to take advantage of exposure to the asset class. CITs are not subject to the same level of Commission oversight as open-end funds and are typically limited to institutional and retirement account investors. Non-retirement retail investors are effectively precluded from investing in CITs. A significant number of retail investors are similarly restricted from investing in private funds because such funds have suitability requirements based, in part, on considerable investor net worth.

Closed-end bank loan funds became available over 30 years ago, and since that time, it has become clear that investors prefer the open-end fund structure. The chart below illustrates this point.

Investors prefer Open-End Funds over Closed-End Funds





Source: Morningstar.

1 For use with SEC only. Not for re-distribution.

Investors Prefer Open-End Bank Loan Pricing

Investors seeking exposure to this asset class prefer the open-end fund structure because these funds are less expensive and trade to fund NAV as compared to closed-end funds. Closed-

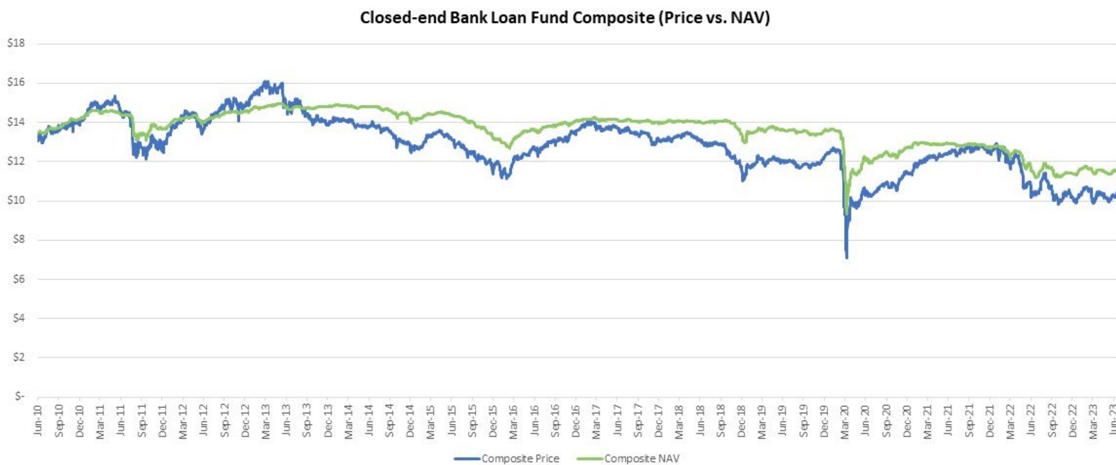
end funds trade on an exchange, offer only limited initial funding, and include higher operational and investment expenses due to their structure and trading. For example, an investor holding $100 in an open-end bank loan mutual fund would only pay $0.58 in management fees on average while an investor holding $100 in a closed-end bank loan fund would pay $0.95 in average management fees.[8] The average closed-end bank loan fund management fee is almost double that of an open-end bank loan fund, charging investors more over the lifetime of their investment. Investors will ultimately pay more for access through closed-end bank loan funds.

Investors Value the Open-End Bank Loan Fund NAV Structure

Because closed-end funds consist of a finite number of assets in an underlying pool, the size of the fund does not change, and investors are therefore unable to benefit from the reduced expenses associated with an increase in fund assets under management. This discount to NAV can occur when the market trading price is lower than the most recently calculated daily NAV. When an investor seeks to liquidate a portion of their position, the price received for their investment will vary depending on the demand for that investment at any given time rather than the actual value of the securities held in the fund. The closed-end vehicle does not provide the greatest benefit to retail investors because of its expense and discounted price. Historically during times of market volatility, the discount to a closed-end fund NAV has intensified, thus further disadvantaging liquidating investors in a time when they may rely on the sale's returns. As illustrated by the chart below, these structural differences make open-end bank loan funds more attractive to investors, including retail investors.

Bank Loan CEFs often trade at a discount to NAV

- **Shareholders are unlikely to realize an investment's value, thus negatively impacting returns**
- **Fund size is limited to IPO dollar amount**



Source: Bloomberg as of July 2023. Equal weighted composite is comprised of four closed-end bank loan funds.

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IV. Recommended Alternatives

[8] See Morningstar Direct Bank Loan Category as of June 2023.

A. 10% Highly Liquid Investment Minimum

Reiterating the comments made in the Fidelity Comment Letter, we believe the Proposal's mandated 10% HLIM is arbitrary and dramatically overstates the amount of highly liquid investments that a fund should reasonably hold each day, as supported by the Commission's data.[9] Consistently managing funds to a perceived worst-case scenario will jeopardize shareholder returns as funds are forced to reposition their portfolios to comply with a rule requirement that is not grounded in fact. Nevertheless, in the interest of preserving the viability of dedicated open-end bank loan funds and in recognition of their unique liquidity risk factors, Fidelity proposes that the Commission adopt a standard 10% HLIM exclusively for bank loan funds. A 10% HLIM for bank loan funds coupled with the liquidity program administrator's discretion to assess a higher HLIM if appropriate is a reasonable alternative to eliminating the less liquid investment category and forcing the elimination of bank loan funds.

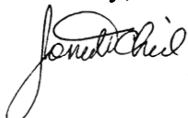
B. Committed Line of Credit

In addition to a required 10% HLIM as discussed above, Fidelity recommends that the Commission require that bank loan funds have available committed lines of credit to enhance fund liquidity. Committed lines of credit allow bank loan funds to bridge the settlement time mismatch, as needed, especially during times of market stress or unexpectedly high redemptions.

* * *

Fidelity would be pleased to provide further information, participate in any direct outreach efforts the Commission undertakes, or respond to questions the Commission may have about our comments.

Sincerely,



cc: The Honorable Gary Gensler, Chair
The Honorable Hester M. Peirce, Commissioner
The Honorable Caroline A. Crenshaw, Commissioner
The Honorable Mark T. Uyeda, Commissioner
The Honorable Jaime Lizárraga, Commissioner

William Birdthistle, Director, Division of Investment Management

[9] Proposing Release at 47.