BlackRock.

February 14, 2023

Submitted via electronic delivery

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 Reporting, File Number S7-26-22

Dear Ms. Countryman:

BlackRock, Inc. (together with its subsidiaries, "BlackRock") respectfully submits the following response to the Securities and Exchange Commission's ("SEC") proposed rule "Open-End Fund Liquidity Risk Management Programs and Swing Pricing; Form N-PORT Reporting" (the "Proposal").[1]

We appreciate the SEC's attention to the important topics of dilution and liquidity risk management for open-end funds. Liquidity risk management is central to managing open-end funds and BlackRock strongly believes in the benefits of swing pricing for mutual funds, where operationalized and available, as an important part of the liquidity risk management toolkit.[2]

For the reasons explained below, however, we cannot support the Proposal, which contemplates a sweeping and complex set of reforms simultaneously that would affect thousands of funds and millions of investors. The Proposal does not adequately address how the proposed measures, including both mandatory swing pricing and significant changes to liquidity risk management, would interact with each other and does not sufficiently identify and account for the potential for harm to US investors and markets. We are concerned that the proposed changes could deprive investors of access to valuable investment options and could negatively impact returns for long-term savers by requiring funds to manage liquidity to an unrealistic set of assumptions and by reducing the ability of managers to exercise the professional judgment that investors seek when investing in funds.

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[1] SEC, Open-End Fund Liquidity Risk Management Programs and Swing Pricing; Form N-PORT Reporting, Rel. No. IC-34746 (Nov. 2, 2022), *available at* https://www.sec.gov/rules/proposed/2022/33-11130.pdf.

[2] Throughout this letter, we refer to mutual funds other than money market funds ("MMFs") as "mutual funds." Swing pricing is not an appropriate tool for money market funds and exchange-traded funds. *See* BlackRock's comment letter on the proposed rule "Money Market Fund Reforms," *available at* https://www.sec.gov/comments/s7-22-21/s72221-20123289-279592.pdf; BlackRock, Swing Pricing–Raising the Bar (Sept. 2021), *available at* https://www.blackrock.com/corporate/literature/whitepaper/spotlight-swing-pricing-raising-the-bar-september-2021.pdf ("Swing Pricing–Raising the Bar").

We look forward to engaging constructively with the SEC and its staff on these topics. We also strongly urge the SEC to reassess its approach to ensure that it has had the benefit of robust dialogue with stakeholders and that any reforms it pursues will benefit investors and improve resiliency.

Executive Summary

Liquidity Rule Modifications

We understand that the SEC believes that the market turbulence of March 2020 compels it to revisit the liquidity rule just four years after it became effective. BlackRock generally supports revisiting rules periodically to determine whether adjustments or updates are needed due to evolving market conditions. However, US mutual funds demonstrated their resilience in response to the March 2020 events and met redemption requests despite challenging market conditions and without the use of extraordinary risk management tools.[3] Therefore, we submit that the Proposal is disproportionate in its response to the events of March 2020, and we are concerned that certain aspects of the Proposal would impose unwarranted limitations on investor choice and access to certain asset classes, disrupt capital markets, hamper prudent portfolio management, and impact portfolio performance.

Accordingly, we recommend that the SEC not adopt the proposed changes. If the SEC moves forward, we provide the following observations and recommendations to better calibrate the Proposal while avoiding more severe unintended consequences.

- **The SEC should maintain the reasonably anticipated trade size.** We do not support the use of the proposed 10% stressed trade size as this would result in day-to-day open-end fund ("OEF") liquidity management that assumes an extreme level of market stress, is out of step with prudent risk management and would unnecessarily hamper long-term investor returns as funds would maintain excess liquidity that is unnecessary in nearly all scenarios.

- **The SEC should retain the current categorization of "less liquid" investments** because the proposed change would largely eliminate investor access to certain asset classes through OEF products and would be disruptive and harmful to bank loan markets and to the companies that rely on such financing. Further, this change is unnecessary and unsupported as the Proposal discounts important facts concerning the ability of bank loan funds to manage their liquidity risks.

- **We agree that certain elements of the Proposal reflect reasonable adjustments,** including expanding the current "illiquid investment" category to include investments priced using unobservable inputs significant to the overall measurement; and codifying the Commission's position that the term "convertible to cash" in Rule 22e-4 means "convertible to US dollars."

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[3] BlackRock, Lessons from COVID-19: Liquidity Risk Management is Central to Open-End Funds (Nov. 2020), *available at* https://www.blackrock.com/corporate/literature/whitepaper/viewpoint-lessons-from-covid-19-liquidity-risk-management-central-open-ended-funds-november-2020.pdf ("Lessons from COVID-19").

- **The SEC should revise its proposed approach to the value impact standard with respect to exchange-traded investments and not adopt the approach with respect to non-exchange traded investments.** In addition, when determining whether a fund can convert an investment to US dollars without significantly changing the market value of the investment, the liquidity rule should permit the fund to reduce any anticipated change in market value by the market impact factor (applied to the trade size assumption).

- **Managers should retain the ability to use asset class classification in appropriate circumstances.** In particular, the SEC should continue to allow asset class classification where there is limited available real-time price data, or where funds otherwise determine to treat certain securities or security types as per se illiquid. For certain asset classes (particularly fixed income asset classes), information about an instrument's asset class as a whole is more indicative of the liquidity of investments in the class than idiosyncratic factors related to individual investments.

- **The SEC should not adopt a 10% uniform highly liquid investment minimum ("HLIM").** We believe that the current HLIM framework is robust and permits funds to establish HLIMs that are appropriate for the asset class of each fund. The SEC has not established why this amendment, which could significantly change the risk-return profile of funds and unnecessarily interfere with prudent portfolio management, is necessary. Should the SEC adopt this change, it should establish a lower HLIM for those exchange-traded funds ("ETFs") that are currently subject to an HLIM requirement to acknowledge the degree to which each ETF meets redemptions in-kind.

Mandatory Swing Pricing and a Hard Close

Asset managers have used swing pricing as an anti-dilution tool for mutual funds, other than money market funds and exchange-traded funds ("ETFs"), in major fund jurisdictions for over twenty years. Based on this experience, BlackRock agrees with the SEC that, for mutual funds, swing pricing is an effective tool for mitigating dilution where it can be operationalized effectively.[4] Swing pricing can be effective in particular because it provides investors with an incentive to spread out share purchases and redemptions over time and protects investors who are not purchasing or redeeming fund shares from the potentially dilutive behavior of others who are through externalizing the related trading costs. Studies have suggested that funds employing swing pricing typically exhibit better long-term investment returns than equivalent funds not using swing pricing or other anti-dilution mechanisms.[5]

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[4] In contrast, we do not believe the implementation of swing pricing for MMFs will achieve the goal of protecting against first-mover advantage while maintaining the usefulness of MMFs for participants in the industry. *See* BlackRock's comment letter on the proposed rule "Money Market Fund Reforms," *available at* https://www.sec.gov/comments/s7-22-21/s72221-20123289-279592.pdf.

[5] Association of the Luxembourg Fund Industry, Swing Pricing Update (July 2022), *available at* https://www.alfi.lu/getattachment/3154f4f7-f150-4594-a9e3-fd7baaa31361/app_data-import-alfi-alfi-swing-pricing-brochure-2022.pdf; Proposal at 94-95.

BlackRock continues to support efforts to encourage the take-up of swing pricing for mutual funds across all jurisdictions.[6] We cannot, however, support the approach described in the Proposal. As the Proposal acknowledges, swing pricing has not gained traction in the US because implementation would require significant changes to the US fund ecosystem, including the systems and business practices of intermediaries and retirement plan recordkeepers. These are changes that asset managers cannot make without wider cooperation among all of these important stakeholders.

Accordingly, we recommend that the SEC reconsider the Proposal. The SEC should instead spearhead a collaborative, stakeholder-focused process to address the barriers to operationalizing swing pricing in the US. We provide the following observations and recommendations on this approach.

- **The SEC should organize working groups to help identify the major challenges that need to be overcome in order to encourage take-up of swing pricing**. Such working groups could include SEC staff, trade groups, investor representatives, intermediaries, plan recordkeepers and asset managers.

- **The working groups should focus on several key areas in order to better inform potential SEC action and ensure the necessary public input and engagement**, including:

  (1) the practical challenges and potential solutions for implementing swing pricing, including dependencies and appropriate staging of changes;

  (2) the importance of allowing managers more discretion on key terms, such as the use of partial swing pricing;

  (3) whether regulatory changes could facilitate voluntary adoption in the US by, for example, ensuring that managers are not unfairly exposed to liability for good faith estimates;

  (4) the costs and benefits of the various alternative anti-dilution mechanisms discussed in the Proposal; and

  (5) how costs can be reduced, managed and allocated so that funds, shareholders and other stakeholders are not adversely or unfairly affected by implementation of swing pricing or alternative anti-dilution mechanisms.

In addressing these challenges, much is at stake. For example, changes to the US fund ecosystem, if not carefully designed, planned and executed, risk resulting in unpredictable, and potentially significant, unintended shifts in how investors access and use investment products. These impacts could be felt across a wide range of investments, including fund of fund arrangements, investments held through 529 plans and 401(k) plans, and variable products. Investors could also find that they face an uneven playing field based on the channel through which they invest in a mutual fund. These concerns are

[6] *See* Swing Pricing–Raising the Bar; *see also* Lessons from COVID-19.

also particularly acute where mutual funds operate alongside other types of investment vehicles because any changes to the ecosystem would necessarily implicate and impact these other vehicles. This, in turn, would have profound consequences for US retirement plan participants and disrupt both investor expectations and established business practices. These changes would come with significant direct and indirect costs, including costs that will be passed through to investors, and which will almost certainly be greater if the SEC forces rather than facilitates change.

Reporting Requirements

- **BlackRock remains opposed to public reporting of aggregate liquidity classifications.** Notwithstanding the proposed liquidity rule amendments and funds' experience with liquidity classifications since 2019, public reporting of aggregate liquidity classifications remains subject to the same concerns that previously convinced the SEC to rescind this aspect of Form N-PORT's liquidity reporting framework. The SEC's proposed changes to the liquidity rule do not overcome previously-acknowledged concerns that variations in liquidity classification methodologies and assumptions would lead to investor confusion and misunderstanding of aggregate liquidity classification data.

- **The SEC should allow more than 30 days to file Form N-PORT in order to permit appropriate data review and correction and to reduce errors.** Form N-PORT has grown in complexity since the SEC first adopted the form, and data quality reviews are an increasingly important part of the process, both for reporting funds and for the SEC. Accordingly, the SEC should allow at least 45 days after month end for filing Form N-PORT in order to permit appropriate data review and correction and reduce the potential for errors in reporting.

- **The proposed requirement to report portfolio holdings on Part F of Form N-PORT for ten months each year is unnecessary and should not be adopted.** We are not aware of investor demand for this information, and the Proposal does not consider reasonably available alternatives for providing this information without the substantial burden of the proposed approach.

Transition Periods

- **If the SEC moves forward with final action rather than first engaging with stakeholders, BlackRock strongly urges the SEC to at least provide longer transition periods in light of the scale and complexity of the proposed changes**. With respect to the changes to the liquidity rule, BlackRock suggests that a transition period of at least three years following the effective date would be more appropriate. With respect to mandatory swing pricing and a hard close, we cannot reasonably recommend an appropriate transition period because the technological, operational and organizational challenges require numerous parties to converge on solutions. Even a period of three years or more is likely to prove inadequate if the SEC does not engage stakeholders in extensive planning and coordination before finalizing any rule.

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I. Liquidity Risk Management Rule Proposals

BlackRock appreciates the SEC's efforts to further tailor the OEF liquidity risk management framework to today's markets. We support revisiting rules periodically to determine whether adjustments or updates are needed, and we understand that the SEC believes that the market turbulence of March 2020 compels it to revisit this rule just four years after it became effective. While BlackRock does not believe the events of March 2020 should be viewed as necessitating changes to the rule, if the SEC determines to adopt a revised rule, BlackRock agrees that certain elements of the Proposal reflect reasonable adjustments. These include:

- Expanding the current "illiquid investment" category to include investments priced using unobservable inputs significant to the overall measurement; and

- Codifying the Commission's position that the term "convertible to cash" in Rule 22e-4 means "convertible to US dollars."

In other respects, however, we submit that the Proposal is disproportionate in its response to the events of March 2020. We are concerned that certain aspects of the Proposal would impose unwarranted limitations on investor choice and access to certain asset classes, disrupt capital markets and hamper prudent portfolio management. Our recommendations below aim to better calibrate the Proposal while avoiding more severe unintended consequences that could negatively impact investors.

Replacing reasonably anticipated trade size with a 10% stressed trade size – resulting in day-to-day OEF liquidity management that assumes an extreme level of market stress – is out of step with prudent risk management and would unnecessarily hamper long-term investor returns as funds would maintain excess liquidity that is unnecessary in nearly all scenarios.

The proposal to mandate an assumed sale of 10% of fund net assets by reducing each investment by 10% in determining liquidity classifications would unnecessarily impose an assumption of extreme, prolonged market stress onto daily liquidity management and would result in nearly all funds greatly understating their liquidity profiles. In view of existing Rule 22e-4 protections, including the 15% limit on illiquid investments, and other proposed changes to the rule, the 10% stressed trade size proposal would lead to considerable constraints on portfolio management. As a result, shareholders, who have made risk-return judgments in allocating investment dollars to OEFs, including judgments concerning liquidity risk, would experience a product fundamentally misaligned with those independent risk-return determinations.[7] Requiring

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[7] *See* BlackRock, Comment Letter, Open-End Fund Liquidity Risk Management Programs; Swing Pricing; Re-Opening of Comment Period for Investment Company Reporting Modernization Release (Jan. 2016), *available at* https://www.sec.gov/comments/s7-16-15/s71615-36.pdf ("BlackRock 2016 Letter") at 2 ("Unlike bank deposits, the liquidity afforded by a mutual fund does not entail a guaranteed price or [NAV] to shareholders upon exit. In considering liquidity risk, it is necessary to remember that amongst the risks borne by mutual

funds to manage their liquidity to a permanent level of market stress would result in funds maintaining excess liquidity that is unnecessary in nearly all scenarios and would result in reduced long-term returns for shareholders. In addition, the selection of 10% appears to be arbitrary rather than a carefully-calibrated balancing of risk management against the impact on portfolio management.[8]

The SEC should instead consider more targeted adjustments to the "reasonably anticipated trade size" ("RATS") mechanism. For example, the SEC could provide guidance for establishing RATS by reference to a fund's historic flow experience that allows for qualitative adjustments (with documented bases) and that may take into consideration investor concentration.

However, if the SEC determines to replace the RATS concept with a stressed trade size presumption, it should establish a minimum that is more congruous with reasonably cautious liquidity management, such as 3% for mutual funds and a lower presumption for ETFs calibrated to acknowledge the degree to which an ETF meets redemptions in kind.[9] The SEC should also permit managers to use higher presumptions on a fund-by-fund basis where they deem it appropriate in accordance with factors (such as historical redemption data and the concentration or diversity of the fund's shareholder base, where known, among others) described in SEC guidance. It would be helpful for such guidance also to address setting trade size presumptions for funds with limited operating histories.

Redefining "less liquid" investments as "illiquid" would largely eliminate investor access to certain asset classes through OEF products and would be disruptive and harmful to bank loan markets and to the companies that rely on such financing.

The Proposal would expand the "illiquid investment" category to include those investments currently classified as "less liquid." BlackRock strongly opposes this proposed change. We agree with other commenters that this significant and abrupt change would largely eliminate investor access to certain asset classes through OEF products (and, thus, eliminate certain investors' access to such asset classes altogether). Bank loan funds provide investors with access to fixed income exposures that allow them to diversify their portfolios, and many investors would not have access to substitutes.

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fund shareholders in return for the expectation of earning attractive investment returns, is that their ability to realize the 'intrinsic value' of their investment may be challenged during periods of market distress. Markets typically offer a return as compensation for relative illiquidity. This is an immutable aspect of capital markets. This resultant risk, amongst many others, is clearly disclosed in a fund's constituent documents.").

[8] The only explanation the Proposal provides is that its analysis of weekly flows shows "outflows of 6.6% occurred 1% of the time in a pooled sample across weeks and funds." Proposal at text accompanying note 82. While the Proposal asserts that "weekly outflows at the 99th percentile is a useful approximation of the level of outflows funds may experience in future stressed conditions," it does not justify using a number based on weekly outflows or provide an explanation for the jump from 6.6% to 10%. Proposal at text accompanying note 83.

[9] ETFs that do not operate as in-kind ETFs may meet redemptions partially in-kind with the balance in cash. The stressed trade size for an ETF should be applied to the proportion of ETF holdings that cannot be delivered in kind. For example, if we assumed mutual funds should use a stressed trade size of 3%, an ETF with one-third of its redemption basket exposed to securities that cannot be delivered in kind would have a stressed trade size of 1%.

This change to the classifications is, moreover, a disproportionate and unresponsive step in view of bank loan funds' decades-long record of meeting redemptions, including throughout the March 2020 and December 2018 stress periods.[10] Indeed, the Proposal appears to discount the effectiveness of liquidity risk management by OEFs that predominantly invest in less liquid investments. However, these funds employ a range of tools to manage liquidity effectively. In addition to the protections designed in direct relation to Rule 22e-4 (such as HLIMs and the 15% limit on illiquid investments), other tools, such as dedicated and committed lines of credit, contribute to these products' liquidity risk management.[11] The Proposal dismisses the use of lines of credit with a conclusory claim that they have become more difficult to obtain. This does not explain, however, why the SEC would ignore the use of lines of credit as a valuable liquidity risk management tool for those funds that have them. The Proposal also does not consider that OEFs have been able to obtain faster settlement when desirable, and it does not account for the potential for contractually expedited settlement or the use of participation interests to accelerate loan settlement for OEFs as needed.

Further, while effectively proposing to eliminate certain strategies from the retail market, the SEC has not fully considered the market impacts of this change. For example, while the Proposal discusses bank loan funds, it does not include a comprehensive analysis of impact on other strategies within the debt markets, the change in the risk-return profile for such funds, the impact on the broader market of the elimination of a funding vehicle, and the impact on retail investors of lesser product choice. We urge the SEC to undertake a more robust study of these effects particularly because, as noted above, the events of March 2020 do not support such broad and rapid changes to the liquidity risk management framework for OEFs.

If, despite these significant concerns, the SEC determines to include "less liquid" investments within the "illiquid investment" category, it should permit an implementation period of at least three years following the final rule's effective date in order to spread out the adverse impact of this change over a longer period.

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[10] Although "bank loan funds had outflows of $12.4 billion (or 13.4% of prior period assets in these funds)" during March 2020, no bank loan fund failed to meet redemption requests during this period. *See* Proposal at 25, 62 ("[B]ank loan funds were able to meet redemption requests during March 2020"); Lessons from COVID-19 at 26 ("[I]n recent stress scenarios – December 2018 and March 2020 – [bank loan funds] have met 100% of redemption requests.").

[11] To the extent the SEC determines not to include "less liquid" investments within the "illiquid investment" category, liquidity risk management program administrators should be permitted to count dedicated and committed lines of credit favorably in the HLIM calculation. We acknowledge the SEC's previous rejection of a one-for-one reduction in HLIM by the amount of an available line of credit, but we urge the SEC to consider permitting a fund's dedicated and committed line of credit to count toward highly liquid investments for purposes of HLIM calculation. *See* Investment Company Liquidity Risk Management Programs, Rel. No. IC-32315 (Oct. 13, 2016), *available at* https://www.sec.gov/rules/final/2016/33-10233.pdf ("2016 Liquidity Rule Release") at 212-213.

If the SEC adopts mandatory swing pricing (or another anti-dilution mechanism) that takes into account market impact, it should harmonize its approach to the value impact standard. The Proposal did not take account of the interaction between the rules, ignoring the effect that externalizing market impact costs would have on the fund's ability to obtain liquidity without incurring a significant change in the value of an investment on disposition.

Both the Proposal and the current liquidity rule define liquidity, in part, with reference to whether the disposition of an investment would significantly change its market value. A simple assessment of this potential change in market value might only compare the current value to the price that a fund expects to realize should it dispose of an investment in a reasonably anticipated trade size or (under the Proposal) a stressed trade size. However, if the rule defines liquidity based on a fund's ability to dispose of an investment without experiencing a significant value impact, then the rule also should allow funds to classify investments taking into account the ability to externalize market impact costs.[12] After all, as the SEC has explained, the value impact component of liquidity classifications relates to dilution of non-redeeming shareholders in addition to the basic ability to meet redemption requests.[13] Where an anti-dilution mechanism is in place that accounts for market impact, liquidity classifications should not be required to ignore that mechanism.

Accordingly, if the SEC adopts mandatory swing pricing (or another anti-dilution mechanism) that permits or requires a fund to externalize market impact costs, it should harmonize its approach to the value impact standard. A harmonized approach would permit a fund to reduce any anticipated value impact by an amount equal to the market impact factor calculated pursuant to proposed rule 22c-1(b)(2)(iii)(A) multiplied by the dollar value of dispositions implied by the stressed trade size assumption under proposed rule 22e-4(b)(1)(ii)(B) (or such other trade size assumption as may be adopted).[14] (Supplementally, we observe that properly harmonizing the swing pricing and liquidity rule amendments in this way would largely obviate the need for a value impact standard. Using the proposed stressed trade size assumption, the market impact threshold would always be exceeded, so liquidity classifications would always account for the ability to fully externalize market impact costs. More generally, a value impact standard in liquidity classifications is only non-redundant to the extent market impact costs are not

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[12] Market impact under the Proposal is an "estimate of the percentage *change in the value* of the investment if it were purchased or sold," per dollar purchased or sold, multiplied by the amount purchased or sold under the proposed swing pricing rule's pro rata assumptions. *See* proposed rule 22c-1(b)(2)(iii).

[13] *See* 2016 Liquidity Rule Release at 106 ("[I]ncorporating a value impact analysis into liquidity considerations is appropriate because it indicates that liquidity risk for a fund captures not just the risk of being unable to meet redemption requests, but also the risk that a fund could only meet redemption requests in a manner that significantly dilutes the funds' non-redeeming shareholders.").

[14] Market impact under the swing pricing proposal is dependent upon the fund's flows. *See* proposed rule 22c-1(b)(2)(iii)(B) (providing that market impact for an investment is determined by multiplying the market impact factor by the pro rata amount of the investment to be purchased or sold in light of fund flows). In contrast, under the proposed liquidity rule amendments, there would be a uniform trade size assumption independent of fund flows. Thus, absent extraordinary circumstances (flows equal to 10% of NAV), simply using the market impact estimate under proposed rule 22c-1(b)(2)(iii) for the adjustment to value impact that we propose would be to adjust based on a disproportionately small factor. Accordingly, the adjustment should be calculated based on the trade size assumption required under the amended liquidity rule.

externalized – i.e., if funds are permitted to base liquidity classifications on presumed sales that may be less than the market impact threshold.)

The proposed 1% value impact standard is ill-suited to non-exchange-traded investments and would result in artificially lower liquidity classifications for certain investments in certain market environments. Establishing such a low standard also risks unpredictable and harmful market effects because, in some market conditions, large numbers of funds may need to reclassify large numbers of investments contemporaneously.

For many widely-held fixed income asset classes, such as certain securitized products, infrequent trading means that there is limited available real-time price data of the type that would be required to apply the proposed standard with precision.[15] This should not be construed as an indication of illiquidity.[16] As the SEC acknowledges, "bonds are split into many different issues and differ from common shares, where volume is concentrated because there generally is only one class of shares for each issuer."[17] In other words, the nature of pricing information is different for fixed income instruments than for traded equity. To determine the price of traded equity, the most relevant information is often the most recent trades in that equity. In contrast, fixed income instruments are typically buy and hold investments, and the most salient information about the value of a fixed income instrument is typically related to its broad characteristics, like maturity date, tenor and interest rate, rather than instrument-specific trade information. Where real-time prices are not available, funds may need to rely on bid-ask spreads, but the same threshold could not be applied to a test based on bid-ask spreads because the normal market ranges are different from price impact ranges. Accordingly, the SEC should reconsider imposing on non-exchange-traded investments a value impact standard where the data required for application of the standard is often unavailable and is less relevant to non-exchange-traded investments' liquidity.

In addition, the proposed value impact standard would have procyclical effects, ultimately to the detriment of funds, markets and shareholders. Using the proposed 1% value impact standard, we estimate that, on certain days in March 2020, one-third of corporate bonds would have been artificially classified as illiquid despite remaining liquid

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[15] *See, e.g.*, BlackRock 2016 Letter at 13 ("In today's fixed income market, the preponderance of trading is concentrated in large, on-the-run issues, and there are thousands of off-the-run issues that do not trade regularly and are, therefore, not priced in the marketplace.").

[16] *See, e.g.*, BlackRock, Addressing Market Liquidity: A Broader Perspective on Today's Bond Markets (Nov. 2016 (updated and re-issued)), *available at* https://www.blackrock.com/corporate/literature/whitepaper/viewpoint-liquidity-bond-markets-broader-perspective-february-2016.pdf at 16-17 (highlighting "several aspects of the fixed income ecosystem that are missing from today's dialogue," such as "[f]actors that combine to suppress bond turnover statistics, including the large amount of bonds held by central banks, the growing use of lower velocity strategies by corporate [defined benefit] pension plans alongside insurers, and the increasing appeal of index strategies" and "[t]he growing adoption of bond ETFs, which supplement traditional forms of obtaining bond market liquidity through trading of bond ETF shares on equity exchanges"); BlackRock, Addressing Market Liquidity: A Broader Perspective on Today's Euro Corporate Bond Market (Aug. 2016), *available at* https://www.blackrock.com/corporate/literature/whitepaper/viewpoint-addressing-market-liquidity-euro-corporate-bond-market-2016.pdf at 16-17 (pointing out similar aspects of the Euro corporate bond market).

[17] Proposal at 274.

by any reasonable measure. If the standard were 2% or 3%, the proportion of corporate bonds classified as illiquid at that time would fall by roughly 50% and 75%, respectively. In other words, we have seen market conditions that, under the proposed approach, would prevent many funds from being purchasers, and possibly cause them to become sellers, in a falling market. As we saw with fees and gates in the context of money market funds, policy choices embedded in rules can have effects in stressed markets that harm more than help, and tying the hands of managers when assessing value impact is likely to have a similar result.

If the SEC adopts a definition of "significantly changing the market value of an investment" with respect to non-exchange-traded investments, it should adopt a flexible standard that allows funds to take into account data they regard as salient, available and reliable rather than a quantitative standard. In addition, this standard should not be required to factor in both the fund's sale of the asset and broader market moves. Accounting for broader market moves would require funds to make predictions that are inherently uncertain and may also result in procyclical effects where anticipated market declines prompt reclassifications and, ultimately, more dispositions.

If the SEC determines to retain a specific quantitative standard, we would urge the SEC to adopt a more flexible approach that allows for more tailored risk management. For example, based on the analysis of corporate bonds in March 2020 discussed above, we recommend that the SEC not adopt a standard any lower than 3%, exclusive of underlying market movement, for instruments where sufficient real-time price data is available as determined in good faith by the liquidity risk management program administrator. This should also include an alternative, flexible standard permitting the use of other data, such as bid-ask spread data, where real-time price estimates are limited, unavailable or, in the judgment of the liquidity risk management program administrator, less reliable. If the SEC moves forward with this change, it should also permit funds to establish value impact thresholds for non-exchange-traded investments that vary by grouping, such as asset class, subject to an overall maximum value impact standard of at least 3% for any such holding, and couple this approach with the alternative described above.

The SEC should also revise its proposed approach to the value impact standard with respect to exchange-traded investments.

The SEC proposes to define "significantly changing the market value of an investment" with respect to exchange-traded investments by reference to average daily trading volume. We suggest the value impact standard allow for the use of model average daily trading volume. This approach is particularly useful where a security trades on multiple exchanges and model average daily trading volume can provide a more accurate measure than realized average daily trading volume. However, rather than requiring funds to support a layered approach that mixes model average daily trading volume for certain instruments with realized average daily trading volume for others, we recommend permitting the use of model average daily trading volume in all cases. We also propose an adjusted treatment for exchange-traded fund products held as assets in mutual funds, as average daily trading volume does not fully capture these investments' liquidity. For such an investment, a standard that takes into account both secondary market volume and the trading volume of the investment's underlying holdings would present a more accurate picture of the investment's liquidity.

The Proposal would also require treating foreign holidays as zero volume days. The SEC should not adopt this approach, which is inconsistent with the purpose of the look-back standard. For example, many Asian countries observe the lunar new year holiday, which is an extended public holiday that can last for at least five business days. If we treat each day of the lunar new year as a zero volume day and we use 20 days of historical data for assessing liquidity, then five of those 20 days would have been zero volume days as of the first day the market reopens. There is no reason to believe that, because the day of reopening was preceded by an extended holiday, the day of reopening itself would witness anything other than normal trading volumes. Yet the proposed approach would result in the proposed measure of value impact being significantly depressed until the lunar new year holiday rolls out of the 20 day window. OEFs have many tools available to manage liquidity risk through foreign holidays, and artificially depressing their liquidity on days when markets are open is both unnecessary and inconsistent with the actual liquidity of these funds.

The SEC should retain managers' ability to use asset class classification where there is limited available real-time price data, or where funds otherwise determine to treat certain securities or security types as per se illiquid.

As discussed above, for certain asset classes (particularly fixed income asset classes), individual instrument-level real-time price data can be sparse or unavailable. However, this is not indicative of illiquidity. Rather, for these asset classes, data regarding the asset class as a whole are, in fact, more indicative of the liquidity of investments in the class than idiosyncratic factors related to individual investments.[18]

The Proposal is unclear, in explaining the elimination of asset class classification, as to whether the SEC intends to prohibit classifying an investment using information about similar investments even where that is the most salient information regarding the investment's liquidity. If the SEC's goal is simply to require that OEFs have the capacity to classify investments individually but would not restrict OEFs from incorporating class-related characteristics where appropriate, then the SEC should make that intention clear in both the rule text and guidance in the adopting release. The SEC could address this with guidance that funds may establish a hierarchy of classification data sources. Market data regarding individual investments could be at the top of the hierarchy, but funds could be permitted to classify individual investments by utilizing information regarding the investment's asset class where the liquidity risk management program administrator views that information as more salient, reliable or reasonably available.

If the SEC's intention is to require that OEFs take into account only information that is investment-specific when classifying each investment, then we are concerned that the result would be less reliable classifications. Asset class information is a valuable and reliable tool for certain asset classes where individual instrument-level real-time price

[18] *See, e.g.*, Hanouna, Novak, Riley, Stahel, Liquidity and Flows of US Mutual Funds (Sep. 2015), Memorandum prepared for Mark Flannery, Director and Chief Economist of the Division of Economic and Risk Analysis, *available at* https://www.sec.gov/dera/staff-papers/white-papers/liquidity-white-paper-09-2015.pdf at 32 (noting that a certain "liquidity measure works well for US equity funds because it only requires data on daily prices and trading volume, which is readily available for nearly all US equities, and US equity funds hold few assets other than US equities. In comparison, liquidity measures for fixed-income securities are typically more complex and tailored to the data available for each class").

data is sparse or unavailable and will be particularly important if the SEC adopts its proposed changes with respect to stressed trade size and the value impact standard.

Additionally, a fund may determine that certain securities or security types are *per se* illiquid due to particular characteristics, such as (without limitation) regulatory or contractual transfer restrictions, and regardless of value impact expectations, trade size considerations or other data. The SEC should preserve the ability for a fund to deem securities or security types *per se* illiquid without requiring all such securities to undergo instrument-level value impact and trade size analysis.

The SEC should not adopt a 10% uniform minimum HLIM, which is arbitrary, and if it adopts this change, should at least establish a lower minimum HLIM for ETFs calibrated to acknowledge the degree to which each ETF meets redemptions partially in-kind.

The Proposal would impose a uniform minimum HLIM of 10% on OEFs (other than in-kind ETFs). The SEC proposes this change to mirror the stressed trade size amount also set by the Proposal, without explaining why this is a necessary or appropriate amendment. As discussed above, we believe the proposed stressed trade size percentage is not an appropriate uniform metric for liquidity risk management and do not believe importing it into the HLIM requirement would benefit funds or shareholders. We also believe a uniform minimum HLIM across funds is not necessary or appropriate. Such a requirement would not recognize the current, and varied, state of fund liquidity management and would impose a potentially unnecessary obstacle to effectively managing a given fund's level of HLIM that is reflective of the fund's unique characteristics. However, if the SEC moves forward with a uniform minimum HLIM, in our experience even a measure of 5% would represent a conservative standard.

Finally, we note that ETFs that do not operate as in-kind ETFs often meet redemptions partially in-kind with the balance in cash. In contrast, mutual funds generally meet redemptions fully in cash, and such differences should be reflected in the respective products' HLIM requirements. For example, consistent with our recommendation regarding the application of a stressed trade size to ETFs, if the SEC imposes a minimum HLIM for OEFs, the HLIM for an ETF should be applied only to the portion of ETF holdings that cannot be delivered in kind. In this example, if it is assumed that mutual funds have a minimum HLIM of 10% (as proposed), an ETF with one-third of its redemption basket exposed to securities that cannot be delivered in kind would have a minimum HLIM of 3.33%.

II. Mandatory Swing Pricing and Hard Close

We provide comments on key aspects of the Proposal and the alternatives below.

Swing Pricing and Closing Mechanics

The SEC should explore alternatives to a hard close, including the potential for enhancing the availability of indicative flow information.

A significant challenge to adopting swing pricing in the US under the current, "high confidence" estimate standard is obtaining same-day investor net flows early enough to determine whether to swing the NAV and in which direction. In Europe, the hours-long gap in time between cutoff and NAV determination permits much greater certainty around the direction and level of flows by the time funds are valued. In the US, fund valuation and receipt of fund flows data currently are effectively two separate processes, and other commenters have explained in detail why the European operational model cannot simply be imported into the US. The current timing of the distinct valuation and flow processes in the US, in most cases, does not permit certainty concerning fund flows before a fund's NAV is published.

The SEC proposes to address these challenges by imposing a hard close at the time as of which the fund's NAV is calculated (sometimes referred to as its "pricing time"), which is generally 4 p.m. ET. This hard close approach, however, creates a number of additional, acute challenges for implementing swing pricing in the US, and would be disruptive to shareholders, intermediaries and funds. The Proposal would cut off transmission of orders from intermediaries so early in the day that redemption and purchase orders for significant numbers of fund shareholders would be forced into processing at the next day's NAV, despite those orders having been received by an intermediary, acting as agent, before the pricing time. As explained above, such changes risk resulting in unpredictable, and potentially significant, unintended shifts of how investors access and use investment products. In addition, the hard close would create an uneven playing field among investors, even in the same fund, by forcing some investors to bear an additional day of market exposure based solely on the channel through which they invest in a fund.[19] The result would be unfair treatment of similarly situated investors as well as confusion among investors regarding when and how their purchases and redemptions of mutual fund shares would occur.[20]

For these reasons, the stakes are high, and the proposed hard close risks significant costs and disruption to retail investors and others. Accordingly, the SEC should seek input from market participants on developing alternative approaches that could be pursued at substantially lower cost and potential for disruption. This should begin with establishing stakeholder working groups to explore alternatives, including the potential for enhancing the availability of indicative flow information.

The Proposal should allow swing pricing administrators to rely on good faith estimates when determining whether to swing and in which direction.

The Proposal would, similar to the current rule, permit swing pricing determinations to be made based only on "reasonable, high confidence estimates" of flows. If the SEC were to mandate swing pricing, this standard, which has been untested under the current rule, would take on greater significance. By requiring mutual funds to use swing pricing, the SEC would force funds and swing pricing administrators to take on liability for determining each day whether and in which direction to swing. For the reasons discussed

[19] This result also appears inconsistent with the fundamental policy purposes of Section 18(f) and Rule 22c-1, which generally seek to provide equal treatment of similarly situated shareholders and payment upon redemption at the price next computed.

[20] We also agree with the Investment Company Institute that the proposed hard close would adversely affect funds and their shareholders by hampering the ability to appropriately address order cancellations and corrections.

above, we do not believe mandating a hard close is a practical or reasonable approach to addressing this concern, and the SEC should instead explore less costly and disruptive alternatives that take advantage of currently available information.

We have analyzed flow data for our full range of US retail mutual funds over a period of more than a year to assess how often we would have accurately determined whether to swing and in which direction based on currently available flow information. This analysis shows that, for these funds, without a need for a hard close, current flow information could enable accurate determinations about whether to swing and the direction of swing to be made the vast majority of the time.[21] On the other hand, the analysis also confirms that these determinations would, a small percentage of the time, result in a determination to swing that would have been different if all flow information were known. Although the results improved significantly using information up to and including 6 p.m. EST, they did not change materially based on incorporating information received later – i.e., for these funds, investor behavior did not differ materially between the retail and brokerage channels that tend to transmit orders earlier from the retirement channel. Therefore, it may be possible for US asset managers to calculate swing pricing with a *reasonable* degree of confidence in the accuracy of estimates based on currently available information. At the same time, both the current and proposed requirement for "high confidence estimates" imply a liability standard that serves as a significant deterrent to implementation because it is almost certain that, in a small number of instances, the available information would result in swing determinations that would be different with information obtained after the fact.

This analysis highlights that there is a tradeoff between the need for accuracy and the cost of implementation. If the SEC insists on perfect, or near perfect, accuracy of the flow information for swing determinations and imposes a standard of liability consistent with that, then the result would be a staggering cost of implementation, including an ongoing disadvantage to mutual funds arising from early order cut-offs. On the other hand, if the SEC were to recognize that funds and swing pricing administrators could achieve much of the benefit of swing pricing using reasonably designed good faith, rather than "high confidence", estimates, then implementation may be possible at much lower costs. This modification, which based on our analysis described above we do not believe would expose investors to additional risk, might then spur voluntary implementation.

In addition, as we commented in 2016, the SEC should further provide a safe harbor from liability for differences between estimates in connection with determining whether to swing, the direction of swing and the amount of any swing factor and information that becomes available after the fact, provided that reasonably designed swing pricing procedures are followed properly. The SEC declined to take this approach in

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[21] This analysis focused on flows and did not look at the separate considerations around establishing the swing factor.

2016, and we believe this has significantly discouraged funds that would otherwise be inclined to explore swing pricing from moving in that direction.[22]

In addition, the SEC should further reduce the liability risks to asset managers related to using estimates by permitting partial swing pricing on both net redemptions and net purchases. A requirement to swing every day that a fund experiences net redemptions significantly increases the potential for differences between estimates and information observed after the fact by requiring the swing pricing administrator to make determinations when smaller differences between initial and final information about flows could result in differences.

BlackRock believes that the SEC should consider this substantial barrier to implementation, with the input of working groups, in order to consider ways to facilitate the uptake of swing pricing on a voluntary basis.

Swing pricing administrators should be permitted to establish the swing threshold on both days with net redemptions and days with net purchases.

The Proposal would require the application of a swing factor every day that a fund experiences net redemptions, with no discretion to establish a swing threshold. The Proposal would, however, permit a fund's swing pricing administrator to set a swing pricing threshold (to a maximum of 2%) for net purchases that it determines would be appropriate to mitigate dilution.

Swing pricing administrators should be permitted to establish a swing threshold for days that a fund experiences net redemptions so that the fund is required to adjust its net asset value per share ("NAV") by a swing factor only when those net redemptions exceed such threshold. This "partial swing pricing" has a lower impact on NAV accounting volatility, given that the price is not necessarily swung on each valuation date, and is widely adopted in many other jurisdictions that have operationalized swing pricing.[23] The volatility that would result from full swing pricing on days with minimal net redemptions could be considered artificial and is not reflective of realized underlying asset volatility. Additionally, having a threshold recognizes that ordinary daily flows can be managed with no significant market impact and reserves swing pricing for those instances when it is most valuable as an anti-dilution mechanism. While there may be instances where a swing

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[22] *See Investment Company Swing Pricing* SEC Rel. Nos. 33-10234; IC-32316 (Oct. 13, 2016), *available at* https://www.sec.gov/rules/final/2016/33-10234.pdf at note 189 ("We decline to provide such a safe harbor given the facts and circumstances nature of this determination.") ("Swing Pricing Adopting Release"). That release provided that, "if a fund, pursuant to reasonably designed policies and procedures, determined with reasonable high confidence that it should apply swing pricing based on estimated information obtained after reasonable inquiry, the fund would not need to treat the application of swing pricing as a pricing error if it turned out, after the fact based on final data, that the swing threshold had not been crossed; similarly, the fund would not need to treat the failure to apply swing pricing as a pricing error if it turned out, after the fact based on final data, that the swing threshold had been crossed." Swing Pricing Adopting Release at note 190. This statement accurately recognized that determinations made consistent with reasonably designed policies and procedures should not be treated as errors, but by failing to go further in establishing a safe harbor, the 2016 rulemaking established an unreasonable impediment to implementing swing pricing.

[23] *See* BlackRock, Swing Pricing–The Dilution Effects of Investor Trading Activity on Mutual Funds (Oct. 2020), *available at* https://www.blackrock.com/corporate/literature/whitepaper/swing-pricing-dilution-effects-of-trading-activity-on-mutual-funds-october-2020.pdf.

pricing administrator views a full swing approach as the most appropriate for a fund, the swing pricing administrator should have the ability, in the exercise of its fiduciary duties, to make a judgment about whether full or partial swing pricing is in the best interest of each fund and its shareholders. This is not unlike the discretion that fund boards and valuation designees are charged with exercising in connection with determining fair value in good faith, and there is no reason to take an approach with respect to the application of swing pricing that deprives funds and their shareholders of this professional judgment.

We submit that most of the benefits of swing pricing would be achieved in a partial swing pricing regime and, in any case, where a particular fund would benefit from full swing pricing, the swing pricing administrator has incentives to set a threshold that is low or zero.

We also appreciate that, in proposing to establish an upper bound for the swing threshold, the SEC was likely seeking to ensure that its goal of operationalizing swing pricing would not be frustrated through excessively high swing thresholds. Accordingly, if the SEC adopts mandatory swing pricing, establishing a maximum swing threshold requirement for net redemptions at least as high as that proposed for net purchases would be more appropriate than allowing no threshold. The swing pricing administrator would be in the best position to determine the appropriate threshold for a particular fund, and funds and shareholders should benefit from the swing pricing administrator's professional judgment as applied to the circumstances of each fund.

The SEC should make additional changes to the Proposal in light of the limitations it would impose on order processing.

The SEC should expressly permit swing pricing administrators to use the previous day's unswung NAV for estimating unit order amounts. Some orders are submitted based on a number of shares, while estimated net flows are calculated on a dollar basis. Based on a review of data, we believe that, with an immaterial number of observed exceptions, this would not materially affect accuracy of determinations regarding whether and in which direction to swing. Accordingly, although funds may ultimately find that, with systems changes, these estimates could be made with same-day NAV, permitting this alternative could reduce the amount of changes to existing market practices and infrastructure that need to be managed in the first stage of implementation without reducing the intended benefits.

When determining the swing factor, the SEC should permit swing pricing administrators to decide whether market impact costs are material for each fund rather than requiring consideration of market impact costs at mandatory thresholds for net redemptions or net purchases. If the SEC requires thresholds, establishing the thresholds should be in the discretion of the swing pricing administrator. The SEC should also acknowledge that the thresholds may appropriately vary by fund.

The Proposal would require the swing factor to account for market impact costs at a threshold of 1% for net redemptions and 2% for net purchases or, in either case, at a lower threshold that the swing pricing administrator determines. Swing factors are based on anticipated transaction costs for transacting in a portion of the fund's assets, which may include cost that are explicit (e.g., taxes, levies, and broker fees) and implicit (e.g., bid-ask spreads and market impact). Each of these will vary according to the fund's asset class or sector and the net flows the fund must accommodate and in response to changes in market conditions. Understanding and anticipating these costs – in particular, market impact costs – requires informed judgement, and for some securities the line between explicit and implicit costs may be less clear.[24]

As a result, determinations regarding swing pricing and the swing factor cannot be captured in a one-size-fits-all model and require continual manual oversight and input. Each fund's appropriate swing thresholds and swing factors will depend on a number of factors, including fund size, the dealing costs and liquidity of the underlying markets and the investment universe in which the fund invests. This is particularly true with respect to market impact costs because of the significant amount of judgment necessary to determine whether these costs, on a given day, are likely to result in significant shareholder dilution and to estimate the amount of such costs. Accordingly, the rule should not specify thresholds at which the swing pricing administrator is required to account for market impact costs and should, instead, permit the swing pricing administrator to decide whether market impact costs are material for the fund. If the SEC requires thresholds, the swing pricing administrator should have discretion to establish and review appropriate thresholds on an ongoing basis.

In-kind purchases and redemptions should receive the unswung price because they do not present the same potential for dilution to remaining investors as cash purchases and redemptions.

The Proposal would exclude in-kind purchases and redemptions from fund flows for purposes of determining whether swing thresholds are met, but these orders would still receive the swung price. Although in-kind purchases and redemptions are less common among mutual funds than ETFs, those that occur similarly allow mutual funds to externalize certain transaction costs without the use of market pricing mechanisms, such as swing pricing. We, therefore, believe that in-kind purchases and redemptions in mutual funds should be encouraged. However, if a shareholder transacting with the fund in-kind were to receive or pay the swung NAV, the fund would be charging the shareholder for costs the fund did not bear. Accordingly, the SEC should permit funds to, as applicable and where operationally feasible, process the orders of shareholders engaging in in-kind purchases or redemptions using the unswung NAV even if, on the relevant day, the fund utilizes swing pricing.

<u>Anti-Dilution Alternatives Discussed in the Proposal</u>

The Proposal discusses a variety of potential anti-dilution mechanisms that the SEC described as alternatives to mandatory swing pricing. Several of the alternatives to swing pricing described in the Proposal could also serve as effective anti-dilution tools. However, to be effective, we believe they would require information similar to that needed to implement swing pricing and would, therefore, pose many of the same challenges to implementation. Accordingly, while we would support the SEC making available to funds a

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[24] *See* Swing Pricing–Raising the Bar.

variety of anti-dilution tools, we would have concerns with the SEC proceeding to adoption on any of the alternatives identified in the Proposal for the same reasons discussed above

Properly structured, dynamic liquidity fees can operate in a manner that is economically similar to swing pricing for mutual funds.

The Proposal requests comment regarding liquidity fees as an alternative to swing pricing.[25] We agree that liquidity fees could achieve similar benefits for mutual funds, in terms of addressing potential dilution, as swing pricing. The Proposal describes a spectrum of liquidity fee approaches, ranging from dynamic fees that are adjusted regularly and static fees that are established less frequently. If the SEC were to require dynamic liquidity fees adjusted on a frequent basis, it could present additional operational challenges. The existing mechanisms for charging fees through intermediaries are based on established fee schedules and are not designed for frequent adjustment of the amounts that may be charged.

We believe that, if the SEC pursues liquidity fees, it should permit funds to use a hybrid approach. In other words, the SEC should not require the fund to establish the liquidity fee daily or at any other set frequency. Instead, the SEC should permit the fund to set a standard liquidity fee based on historical data, subject to periodic review (e.g., monthly or quarterly).

If the SEC determines to adopt liquidity fees, we would urge it to consider the concerns we have raised above regarding reliance on good faith estimates and changes needed to address various operational challenges. Moreover, consulting with a wide range of stakeholders in advance of any final action would be just as critical for this, and any other alternatives, as for the mandatory swing pricing and hard close proposal.

In addition, if the SEC adopts a rule permitting or requiring funds to impose liquidity fees, it should not require the fees to be included in the prospectus fee table. Unlike fees that reduce a shareholder's net investment, these fees would be designed to align the aggregate price a shareholder pays with the net value of its purchase or redemption. Disclosure concerning the use of liquidity fees would, however, be appropriate elsewhere in fund documents. For example, funds could disclose, in narrative form, the fact that they use liquidity fees and the material terms for the establishment of liquidity fee rates. It may also be appropriate for funds to disclose, in their statements of additional information, the range of liquidity fees used in the prior year.

[25] The Proposal explains that liquidity fees could be "simplified to remain relatively static" or could be dynamic, meaning that they would reflect "certain costs (e.g., spread, other transaction costs, and market impact) a fund is likely to incur to meet redemptions or invest the proceeds from subscriptions based on the direction and magnitude of that day's flows."

Dual pricing is utilized in jurisdictions outside the US and can also be an effective anti-dilution mechanism.

The Proposal also requests comment regarding dual pricing as an alternative to swing pricing.[26] Although we agree that dual pricing can be an effective anti-dilution tool, implementing it in the US would present the same operational challenges as swing pricing. In addition, as the SEC acknowledges in the Proposal, dual pricing would impose additional operational burdens and complexity on fund intermediaries, service providers, and other third parties to accommodate the processing of two NAVs on each date. Accordingly, this alternative would not alleviate the concerns we have raised with the Proposal and, if the SEC adopts a rule permitting or requiring dual pricing, we would urge it to consider the comments above with respect to swing pricing, many of which would also be relevant to dual pricing.

III. Reporting Proposals

Public reporting of aggregate liquidity classifications could have a confounding effect on investors.

Notwithstanding the proposed liquidity rule amendments and funds' experience with liquidity classifications since 2019, public reporting of aggregate liquidity classifications remains subject to the same concerns that previously convinced the SEC to rescind this aspect of Form N-PORT's liquidity reporting framework.

The SEC indicates that its proposed 10% stressed trade size, value impact standard definition and elimination of asset class classifications overcome previously-acknowledged concerns that variations in liquidity classification methodologies and assumptions would lead to investor confusion and misunderstanding of aggregate liquidity classification data.[27] This misunderstands the impact of the SEC's proposed changes to liquidity classification mechanics and underappreciates the subjectivity that remains inherent to estimating "the number of days in which [an] investment is reasonably expected to be convertible to U.S. dollars without significantly changing the market value of the investment [as newly defined], while assuming the sale of 10% of the fund's net assets by reducing [the] investment by 10%."[28]

As discussed in more detail above, the proposed 10% stressed trade size would result in significant understatement of fund liquidity profiles, while the proposed value impact definition for non-exchange-traded investments would introduce considerable difficulty, and thus uncertainty, into the liquidity classification process for these

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[26] The Proposal explains that dual pricing "would quote two prices—one for incoming shareholders (reflecting the cost of buying portfolio securities in the market), and one for outgoing shareholders (reflecting the proceeds the fund would receive from selling portfolio securities in the market)." The Proposal further explains that dual pricing, like liquidity fees, could be simplified to have a constant spread around a fund's NAV or dynamic, meaning it would reflect "spread, other transaction costs, and market impact a fund is likely to incur to meet redemptions or invest the proceeds from subscriptions and based on the magnitude of those flows."

[27] *See* SEC, Investment Company Liquidity Disclosure, Rel. No. IC-33142 (Jun. 28, 2018), *available at* https://www.sec.gov/rules/final/2018/ic-33142.pdf at 8.

[28] Proposal at 46.

investments. The SEC's proposals to hardwire multiple additional considerations into the liquidity classification framework – including average daily trading volume for exchange-traded securities as well as a security's fair value inputs – would further compound the complexity and uncertainty in liquidity classifications, particularly in times of market stress. As such, while the SEC's proposals would impose a rough standardization on certain key parameters involved in the liquidity classification process, the proposals would magnify, rather than reduce, potential confusion and misinterpretation of publicly-reported aggregate liquidity classification data. Moreover, standardizing two key parameters in liquidity classifications does little to reduce the "highly subjective exercise" of forecasting, based on reasonable expectations, the number of days necessary for the sale and settlement of an investment without exceeding the newly-defined value impact standard.[29] In addition, because of the proposed stylized assumptions, the liquidity classifications potentially would become less meaningful to investors as they are less likely to reflect the actual liquidity profile of the fund. The SEC's answer to this subjectivity explains only that other information would be available to contextualize the aggregate data. It does not address the potential confusion and misinterpretation surrounding the aggregate liquidity classification data itself or clarify the complex and subjective exercise involved in making the liquidity classification determinations underlying the aggregate data.

For these and the additional reasons we have previously described, we urge the SEC not to implement public reporting of aggregate liquidity classification data.[30]

The SEC should allow more than 30 days to file Form N-PORT in order to permit appropriate data review and correction and to reduce errors.

Form N-PORT has grown in complexity since the SEC first adopted the form. In the intervening years, the SEC has introduced new and complex reporting items related to the derivatives and liquidity risk management rules, and Form N-PORT stands to grow further in complexity in light of recent SEC proposals (such as the Names Rule proposal).[31] Moreover, numerous reporting items on Form N-PORT require the use of significant judgment in the analyses necessary to produce the reports. These changes, their complexity, and the judgment that the form requires mean that data quality reviews are an increasingly important part of the process, both for reporting funds (who want to avoid errors) and for the SEC (for which data integrity is undoubtedly important). Accordingly, the SEC should allow at least 45 days after month end for filing Form N-PORT in order to permit appropriate data review and correction and reduce the potential for errors in reporting.

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[29] *See* BlackRock, Comment Letter, Investment Company Liquidity Disclosure Proposed Rule (May 2018), *available at* https://www.sec.gov/comments/s7-04-18/s70418-3654324-162418.pdf ("BlackRock 2018 Letter") at 3.

[30] *See id.*

[31] SEC, Investment Company Names, Rel. No. IC-34593 (May 25, 2022), *available at* https://www.sec.gov/rules/proposed/2022/ic-34593.pdf.

The proposed requirement to report portfolio holdings on Part F of Form N-PORT for ten months each year should not be adopted; it is a substantial filing burden to funds without a material corresponding benefit to investors.

Fund shareholders would, without this change, have access to substantial information regarding fund holdings, including the information reported elsewhere on Form N-PORT, information on Form N-CSR, and website disclosures that many funds make. The Proposal presents no evidence that shareholders want, need or would benefit from having portfolio holdings information specifically in the unstructured format of Part F on the frequency proposed, and therefore it is not evident that the resultant costs associated with adding this information to Form N-PORT are justified. The Proposal also does not explore any alternatives to "make the monthly disclosure more useable for investors." Such alternatives could include the SEC providing a reader tool to present Form N-PORT data, which it could build once and make available to investors, rather than impose additional burdens on all Form N-PORT filers most months, or permitting simplified website disclosures. Accordingly, we do not support this change and urge the SEC, if it sees investor demand for this unstructured information, to explore less burdensome alternatives for making it available.

IV. Withdrawal of Guidance

The Proposal lists certain letters or Staff statements that are being reviewed in connection with the proposed amendments. BlackRock believes that the SEC should retain guidance and statements that are not expressly nullified by the amendments. For example, the staff FAQs addressing the liquidity rule and related matters have provided valuable guidance for implementing the current liquidity rule, and the staff should preserve, at a minimum, the FAQs addressing sub-advised funds, exchange-traded funds, pooled investment vehicles and related reporting requirements.[32] We believe such guidance should be retained in the adopting release, and the SEC should explicitly confirm as much to provide clarity to the industry.

For example, the SEC should confirm that funds may continue to rely on current Staff Liquidity FAQs concerning extended holiday closures and Form N-RN and board notification requirements following the adoption of any final rule amendments.[33] The SEC staff has previously indicated that "the staff would not object if a fund does not file Form N-LIQUID [now Form N-RN] for an investment that become illiquid solely due to an extended holiday closure."[34] Extended holiday closures, particularly those in a handful of foreign countries, often affect liquidity classifications, but as the SEC staff recognized, there is minimal or no increase in liquidity risk due to the closures. Filing a Form N-RN, and notifying the fund's board on the one-business-day time frame contemplated under Rule 22e-4 (rather than in advance as contemplated under the guidance), would serve no meaningful purpose even if Rule 22e-4 is amended as proposed. The rationale behind the

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[32] *See* SEC, Investment Company Liquidity Risk Management Programs Frequently Asked Questions (Apr. 10, 2019), *available at* https://www.sec.gov/investment/investment-company-liquidity-risk-management-programs-faq ("Staff Liquidity FAQs").

[33] *See* Staff Liquidity FAQs, Question 34.

[34] *Id.*

SEC staff's current guidance would hold true no matter what any final rule amendments might require of funds, and we therefore recommend that the SEC endorse this position in any final rule amendments.

V. Transition Periods

BlackRock strongly urges the SEC to provide longer and phased transition periods following the effective date in light of the scale and complexity of the changes proposed. BlackRock suggests that a transition period of at least three years following the effective date would be more appropriate for the changes to Rule 22e-4.

With respect to mandatory swing pricing and a hard close, we cannot reasonably recommend an appropriate transition period because the technological, operational and organizational challenges require numerous parties to converge on solutions. We can say confidently that the proposed compliance period would be inadequate and would expose funds and fund shareholders to significant risk of harm. Even a period of three years or more is likely to prove inadequate if the SEC does not engage stakeholders in extensive planning and coordination before finalizing any rule.

In considering appropriate transition periods for the proposed rule changes, the SEC should bear in mind the far-reaching and fundamental nature of the changes, both individually and cumulatively. In addition to the uncertainty of how the proposed measures in this Proposal would interact with each other, the SEC is considering additional regulatory changes which may have material impacts on the broader market ecosystem, including how investments are traded, and those interactions cannot yet be assessed.[35] Accordingly, the SEC should carefully consider appropriate intermediate milestones rather than focusing on pursuing all of these changes based on a single deadline or closely-spaced deadlines.

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We thank the SEC for providing BlackRock the opportunity to provide our comments and suggestions on the Proposal. Please contact the undersigned if you have any questions or comments regarding BlackRock's views.

Sincerely,

John M. Perlowski, CPA
Managing Director

Samantha DeZur
Managing Director

[35] *See, e.g.*, SEC, Shortening the Securities Transaction Settlement Cycle, Rel. No. 34-94106 (Feb. 9, 2022), *available at* https://www.sec.gov/rules/proposed/2022/34-94196.pdf

cc:

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Chair
Securities and Exchange Commission

The Honorable Hester M. Peirce
Commissioner
Securities and Exchange Commission

The Honorable Caroline A. Crenshaw
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