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November 10, 2022

SEC Proposes Liquidity Rule, Swing Pricing, Hard Close, and Form N-PORT Reporting Amendments

[34347]

November 11, 2022

TO: ICI Members
Investment Company Directors SUBJECTS: Audit Committees
Compliance
Derivatives
Disclosure
Distribution
Exchange-Traded Funds (ETFs)
Fixed Income Securities
Fund Accounting & Financial Reporting
Fund Governance
Intermediary Oversight
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Operations
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Risk Oversight
Transfer Agency RE: SEC Proposes Liquidity Rule, Swing Pricing, Hard Close, and Form N-PORT Reporting Amendments

On November 2, 2022, by a 3-2 vote, the SEC approved a proposal that would:

- amend Rule 22e-4 (the "liquidity rule"), which applies to open-end funds;
- require mutual funds to adopt swing pricing; and
- change all Form N-PORT filers' reporting obligations.[1]

If adopted, these proposed changes would significantly affect open-end funds' liquidity risk management programs; mutual funds' pricing conventions and intermediary relationships; and the reporting obligations and public information available for all Form N-PORT fund filers. The changes also would have a significant impact on certain investment strategies employed by open-end funds and impose substantial compliance costs on funds, intermediaries, and others.

We summarize these proposed changes below.

Comments are due 60 days after the release's date of publication in the Federal Register.

Proposed Liquidity Rule and Related Reporting Amendments

The SEC emphasizes its concern for potential dilution of shareholders' interests in open-end funds and states that a defining feature of these funds is the ability of shareholders to redeem their shares on demand. After noting the growth in open-end funds and the volume of redemptions these funds experienced in connection with the shock of the COVID-19 pandemic, the SEC states that it has identified "weaknesses" in funds' liquidity risk management programs and limited use of tools such as redemption fees or swing pricing. The SEC's proposed amendments are designed to "enhance open-end fund resilience in periods of market stress by promoting funds' ability to meet redemptions in a timely manner while limiting dilution of remaining shareholders' interests in the fund."[2]

Proposed Changes to the Rule's Bucketing Requirements

Currently, the liquidity rule requires open-end funds to classify each of their investments into one of four liquidity buckets using a "days to cash/days to sale" framework (depending on the bucket), generally on a monthly basis.[3] The size and "value impact" assumptions that funds use are key bucketing inputs. With respect to size, the rule requires a fund to classify investments based on "sizes that the fund would reasonably anticipate trading." The rule does not prescribe a precise method for determining value impact (i.e., what constitutes a "significant change in market value" of an investment for purposes of bucketing), leaving funds with discretion in this area.

The proposal would make several significant changes to the rule's bucketing requirements. Specifically, it would:

- Change the size assumption by requiring a fund to assume a 10% sale of each investment. This fixed requirement assumes pro rata selling of portfolio investments in response to redemptions and is meant to more accurately represent a "stressed" trade size.
- Impose a minimum value impact requirement by defining "significantly changing the market value of an investment" to mean:
    - For exchange-listed shares, "any sale or disposition of more than 20% of the average daily trading volume of those shares, as measured over the preceding 20 business days."[4]
    - "For any other investment, any sale or disposition that the fund reasonably expects would result in a decrease in sale price of more than 1%."

These changes are meant to prevent funds from over-estimating the liquidity of their investments and improve comparability of classifications.

- Eliminate the asset class classification method.[5] The SEC believes that this classification method is not widely used, and that it is more likely to over-estimate the liquidity of an investment.
- Eliminate one of the four existing buckets (the "less liquid" bucket) and change the definitions for the remaining three:
    - A "highly liquid investment" would mean "any U.S. dollars held by a fund and any investment that the fund reasonably expects to be convertible to U.S. dollars in current market conditions in three business days or less without significantly

  changing the market value of the investment…";[6]
  - A "moderately liquid investment" would mean "any investment that is neither a highly liquid investment nor an illiquid investment"; and
  - An "illiquid investment" would mean "any investment that the fund reasonably expects not to be convertible to U.S. dollars in current market conditions in seven calendar days or less without significantly changing the market value of the investment… . Any investment whose fair value is measured using an unobservable input that is significant to the overall measurement is an illiquid investment."[7] (emphasis added)

The elimination of the "less liquid" bucket, the expanded definition of "illiquid investment," and the other methodological changes described above would increase the assets in the illiquid bucket (in the aggregate). The SEC notes that bank loans are generally classified as "less liquid," and that their settlement times generally exceed seven days.[8] Assuming settlement times remain unchanged, most bank loans would be "illiquid" under the proposed definition.

- Change the method for counting the number of days in which an investment would be convertible to U.S. dollars. With respect to classifying investments, the SEC asserts that funds have been applying "inconsistent practices" when counting days. Funds would be required to "include the day on which the liquidity classification is made in that [day counting] measurement."[9]
- Require daily classification of portfolio investments in liquidity buckets. Generally speaking, this is currently a monthly requirement.[10] The SEC believes that daily bucketing "would reflect current market conditions more accurately and would provide funds with more data for analysis to prepare for future stressed conditions."[11]

Proposed Changes to the Highly Liquid Investment Minimum ("HLIM") Requirements

Currently, a fund must determine a minimum percentage of its net assets to invest in highly liquid investments, based on the factors it uses to assess its liquidity risk. A fund must review its HLIM at least annually. In-Kind ETFs and funds primarily holding highly liquid assets[12] are exempt from this requirement.

The proposal would require funds (still excluding In-Kind ETFs) to "determine and maintain a highly liquid investment minimum that is equal to or higher than 10% of the fund's net assets." The exclusion from this requirement for "primarily liquid funds" would be removed (the SEC notes that most funds currently do not have HLIMs). The SEC believes that "a regulatory minimum of 10% for the highly liquid investment minimum would benefit investors by improving the ability of funds to meet shareholder redemptions in stressed scenarios."[13]

The proposal also would make certain changes to the HLIM calculation. Specifically, a fund would be required to subtract:

- the value of any highly liquid investments that are assets posted as margin or collateral in connection with any derivatives transaction that is classified as moderately liquid or illiquid;[14] and
- any fund liabilities.

These reductions are meant to account for limitations in a fund's ability to use some of its assets to meet redemptions.

Proposed Change to the 15% Limit on Illiquid Investments

The current 15% limit on illiquid investments would be amended to provide that the value of margin or collateral that a fund would receive upon exiting an illiquid derivatives transaction would itself be treated as illiquid for compliance purposes.[15]

Proposed Liquidity-Related Reporting Amendments

Currently, funds' reporting of liquidity classification information on Form N-PORT is nonpublic. If the proposal is adopted, Form N-PORT would be amended to require a fund to report the aggregate percentages of its assets that fall into each of the three liquidity categories.[16] This aggregated bucketing information would be publicly available; investment-specific classifications would remain nonpublic. In explaining this about-face from its 2018 liquidity disclosure amendments,[17] the SEC states, "Our proposed amendments to the liquidity rule, along with the years of experience that funds have gained in complying with the current rule, also have made the concerns the Commission identified in 2018 [i.e., that bucketing information would be subjective, that it would be presented in isolation, and that it would lack the context of other disclosures about the fund] less relevant."[18]

Form N-PORT would be amended in other ways in response to other proposed liquidity rule amendments.[19]

Form N-CEN would be amended to require a fund to provide information about service providers it uses to fulfill the requirements of the liquidity rule.[20]

Proposed Exemptive Order Rescission and Possible Withdrawal of Staff Statements

The SEC also proposes to rescind an exemptive order that relates to the liquidity rule[21] and states that the Division of Investment Management staff is reviewing its no-action letters and other statements addressing compliance with the liquidity rule and Rule 22c-1 to determine which letters and other staff statements, or portions thereof, should be withdrawn in connection with any adoption.[22]

Proposed Swing Pricing and "Hard Close" Amendments

Background

Many types of pooled investment vehicles, including US mutual funds, "mutualize" portfolio transaction costs among fund shareholders. Because of this mutualization, sizable net redemption and purchase activity, and the transaction costs that often follow, have the potential to dilute the value of existing investors' fund shares, absent some means of apportioning transaction costs to those redeeming or purchasing fund shareholders.

Outside the US, some funds use swing pricing to allocate transaction costs to redeeming and purchasing shareholders in certain circumstances. In effect, swing pricing involves a second step in the valuation process, whereby a fund measures daily net purchase or redemption activity, and, when any pre-determined activity threshold (usually expressed as a percentage of the fund's net assets) is exceeded, adjusts (or "swings") the per share net asset value ("NAV") upward (in the case of a net purchase of fund shares, so that transacting shareholders bear the transaction costs from resulting fund purchases of portfolio securities) or downward (in the case of a net redemption of fund shares, so that transacting shareholders bear the transaction costs from resulting fund sales of portfolio securities).

In 2016, the SEC adopted amendments to Rule 22c-1 that permit, but do not require, mutual funds to use swing pricing.[23] To date, no US mutual fund has adopted swing pricing, and the SEC cites as reasons lack of timely flow information to operationalize this tool, implementation costs, and/or US fund investors' unfamiliarity with it.

Description of the Proposed Swing Pricing Amendments

The proposed amendments to Rule 22c-1 would require all mutual funds to use swing pricing. (ETFs and money market funds would continue to be excluded from these amendments.) The SEC believes that required use of swing pricing could benefit investors through improved performance and dilution mitigation.

Aside from this major change in applicability, the proposed swing pricing provisions are much more prescriptive than those adopted in 2016. The key provisions are as follows:

- A mutual fund must establish and implement swing pricing[24] policies and procedures that adjust the fund's current NAV per share by a swing factor[25] if the fund has net redemptions, or if it has net purchases that exceed an identified threshold.
    - In the case of net redemptions, a fund always would apply swing pricing (i.e., without a swing threshold).
    - A fund would include market impact in its swing factor if net redemptions exceed 1% of the fund's net assets (the "market impact threshold").[26]
    - When a fund has net purchases, it would swing its NAV upward—and include market impact—if the amount of net purchases exceeds 2% of the fund's net assets (the "inflow swing threshold").[27]
    - The swing pricing administrator[28] would review daily "investor flow information"[29] to determine if a fund has experienced net redemptions or exceeded another applicable threshold. While the proposed "hard close" requirements described below are meant to result in funds having timely flow information, the swing pricing administrator could make swing pricing determinations based on reasonable, high confidence estimates of investor flows.
    - In determining the swing factor, the swing pricing administrator must make good faith estimates, supported by data, of the costs the fund would incur if it purchased or sold a pro rata amount of each portfolio investment to satisfy the amount of net purchases or net redemptions (i.e., a vertical slice). Calculating the swing factor would differ depending on whether the fund experiences net purchases or net redemptions.
        - For net redemptions, the estimates must include (i) spread costs;[30] (ii) brokerage commissions, custody fees, and any other charges, fees, and taxes associated with portfolio investment sales; and (iii) if the amount of the fund's net redemptions exceeds the market impact threshold, the market impact.[31]
        - For net purchases exceeding 2%, the estimates must include: (i) spread costs; (ii) brokerage commissions, custody fees, and any other charges, fees, and taxes associated with portfolio investment purchases; and (iii) the market impact.
        - The swing pricing administrator would be permitted to estimate costs and market impact factors for each type of investment with the same or

        - substantially similar characteristics and apply those estimates to all investments of that type rather than analyze each investment separately.
        - Unlike the 2016 amendments, there would be no upper limit on the swing factor.
- The fund's board, including a majority of the independent directors, must:
    - Approve the fund's swing pricing policies and procedures;
    - Designate the fund's swing pricing administrator; and
    - Review, no less frequently than annually, a written report[32] prepared by the administrator.
- Also:
    - Recordkeeping requirements would apply.[33]
    - For "master-feeder" fund structures, only the master fund would use swing pricing.
    - A fund with a share class that is an ETF is subject to the swing pricing requirement only with respect to any share classes that are not ETFs.

Proposed Swing Pricing Reporting Amendments

Currently, if a fund were to engage in swing pricing, it would only be required to report on Form N-CEN if the fund engaged in swing pricing during a given year and, if so, the swing factor upper limit established by the fund.

The proposal would remove that Form N-CEN reporting requirement and replace it with a new Form N-PORT reporting requirement to provide information about the number of times the fund applied a swing factor during the month and the amount of each swing factor applied (positive or negative).

Also, the Form N-1A swing pricing disclosure amendments adopted in 2016 would apply to all mutual funds.[34]

Proposed "Hard Close" Amendments

Currently, if an investor submits an order to an intermediary to purchase or redeem fund shares, that order will be executed at the current day's price as long as the intermediary receives the order before the fund's established time for determining the value of its holdings and calculating its NAV (typically 4 p.m. ET). The fund, however, might not receive information about that order until much later, sometimes as late as the next morning.

Proposed amendments to Rule 22c-1 would require a "hard close" for mutual funds. This would provide that a direction to purchase or redeem a fund's shares is eligible to receive the current day's price solely if the fund, its designated transfer agent, or a registered securities clearing agency[35] (collectively, "designated parties") receives an eligible order before the pricing time as of which the fund calculates its NAV. These amendments are designed to support the proposed swing pricing amendments by facilitating more timely receipt of fund order flow information, and help prevent late trading of fund shares.

Specifically, an "eligible order"[36] to purchase or redeem would receive the price for the next "pricing time"[37] after a designated party receives the order. To receive that day's price, a designated party must receive the eligible order before the pricing time. A fund's board still would be required to establish a "pricing time," which for most mutual funds is typically 4 p.m. ET. The intent is that a fund would be able to finalize the pricing of its shares several hours after the pricing time, by calculating the current NAV, applying any swing factor, and finalizing and publishing the fund share price.

The proposal discusses the impacts that these changes would have on order processing, intermediaries and investors, and certain transaction types. It identifies, as potential improvements or benefits: (i) reducing vulnerability to an intra-day operations disruption, if an intermediary submits orders more often or earlier in the day; (ii) elimination of cancellations and corrections that are submitted after the pricing time; (iii) improvement of the confirmation process; and (iv) more timely and accurate information about the fund's daily flows, which would help with portfolio and risk management.

However, the proposal also recognizes a number of other potential problematic impacts, including the following:

- Funds and intermediaries would need to make significant changes to their business practices, including updating their computer systems, altering their batch processes, or integrating new technologies that facilitate faster order submission.
- Retirement plan recordkeepers may face significant challenges with adhering to the proposed hard close requirement.
- The proposed rule would likely cause some intermediaries to set their own internal cut-off times for receiving orders to purchase or redeem fund shares that is earlier than the pricing time established by the fund. Consequently, investors transacting through intermediaries may lose some flexibility in when they may submit orders through an intermediary to receive that day's price. In all likelihood, many investors would experience a significant change in this respect.
- The proposed hard close requirement could extend completion times for certain types of transactions, where the specific number or value of fund shares to be purchased or redeemed is unknown until that day's price is available (e.g., plan loans or withdrawals).
- The proposed hard close requirement could extend the period of time for executing an investor's request to rebalance its holdings to a target asset allocation or model portfolio. It also might affect current order processing for funds of funds.

Other Proposed Amendments to Rule 22c-1

The proposed amendments would retain the requirements of the current rule concerning the frequency and time of determining the NAV, but would reorganize and reword those provisions. And the rule's provision that would allow funds not to calculate their current NAV on days in which changes in the value of the fund's securities will not materially affect the current NAV would be removed, because the SEC believes it is no longer necessary.

Proposed Amendment to Form N-1A Related to the Hard Close

Item 11(a) of Form N-1A would be amended to require, if applicable, that funds disclose that if an investor places an order with a financial intermediary, the financial intermediary may require the investor to submit its order earlier than the fund's pricing time to receive the next calculated NAV.

Potential Alternatives to Swing Pricing and a Hard Close

The proposal also discusses potential alternatives to the proposal's swing pricing and hard close provisions.[38] As alternatives to swing pricing, the proposal discusses the potential relative advantages and disadvantages of liquidity fees[39] and dual pricing,[40] among others. As alternatives to a hard close, the proposal discusses the potential relative advantages and disadvantages of funds' use of indicative flow information from intermediaries,[41] flow estimates,[42] and later cut-off times for intermediaries.

Other Proposed Changes to Form N-PORT Reporting Requirements

The proposal would require registered management investment companies and ETFs organized as unit investment trusts ("N-PORT Filers") to file Form N-PORT on a monthly basis and would make more of those reports publicly available. In addition, the proposal would add certain liquidity and swing pricing items for applicable open-end funds, which we have summarized above, and amend other disclosures in the form.

Form N-PORT Filing and Publication Frequency

The proposal would require N-PORT Filers to file their Form N-PORTs within 30 days after the end of the month to which they relate, and filings would be made public 60 days after the end of such month.[43] Currently, N-PORT Filers file Form N-PORT for each month of a fiscal quarter 60 days after the end of the fiscal quarter.[44] Only information for the third month of each fiscal quarter is made public.

The SEC proposes increasing the frequency of Form N-PORT filings to enhance its ability to better assess quickly developing events or identify early warning signs of potential distress, as the current reporting system provides them information that is at least two, and in some cases four, months out of date.[45] The SEC proposes increasing the number of Form N-PORT filings made public to assist investors make more informed investment decisions.[46]

Form N-PORT

Current

Proposed

Filing Frequency

Generally 4x/Year - N-PORT Filers file an N-PORT for each month of a fiscal quarter 60 days after the end of the quarter.

12x/Year - N-PORT Filers would file an N-PORT 30 days after each month.

Information Publicly Disclosed/Publication Frequency

4 Filings/Year - Only information for the third month of a fiscal quarter is made public (within 60 days after the end of the fiscal quarter).

12 Filings/Year - Information for each month would be made public 60 days after the end of the month.

Additional Proposed Amendments to Form N-PORT

The proposal also would make several other amendments to Form N-PORT. These include:

- Amending items that currently require funds to report return and flow information, including net realized gain (loss) and net change in unrealized appreciation (or depreciation), for each of the preceding three months to require information only for

the month that the filing covers;[47]
- Amending the requirement that a fund attach its complete portfolio holdings for the end of the first and third quarters of the fund's fiscal year, presented in accordance with Regulation S-X, within 60 days of the end of the reporting period to require funds to attach the disclosure for each month (except for the last month of the fund's second and fourth fiscal quarters, which will be available in the fund's annual and semi-annual reports) within 60 days of the end of the reporting period;[48]
- Amending Part D of Form N-PORT to remove language that limits reporting of nonpublic information about individual miscellaneous securities holdings to reports filed for the last month of each fiscal quarter to now allow funds to provide this more detailed, nonpublic information in Part D for each monthly Form N-PORT filing;[49] and
- Amending certain items and definitions related to entity identifiers to allow a fund to report the RSSD ID assigned by the National Information Center of the Board of Governors of the Federal Reserve, if any, for financial institutions that do not have an assigned legal entity identifier.

Transition Periods

The proposal would provide transition periods after the effective date of the amendments to give funds time to comply with the changes, as follows:

- 24 months after the effective date of the amendments, all mutual funds must comply with the swing pricing and related disclosure requirements, and mutual funds, transfer agents, registered clearing agencies, and intermediaries must comply with the hard close requirements.
- The compliance period for all other aspects of the proposal would be 12 months after the effective date of the amendments.

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Notes

[1] Open-End Fund Liquidity Risk Management Programs and Swing Pricing; Form N-PORT, SEC Release Nos. 33-11130; IC-34746 (Nov. 2, 2022) (the "proposal"), available at www.sec.gov/rules/proposed/2022/33-11130.pdf. Chair Gensler and Commissioners Crenshaw and Lizárraga voted for the proposal, and Commissioners Peirce and Uyeda voted against it.

[2] Proposal at 12.

[3] "In-Kind ETFs" are not subject to this bucketing requirement but are subject to the rule's 15% limit on illiquid investments.

[4] The proposal would permit a stricter limitation (e.g., 15%). See proposal at n.89.

[5] Currently, a fund may classify its investments according to their asset classes. However, a fund must separately classify and review any investment within an asset class if the fund or its adviser has information about any market, trading, or investment-specific considerations that are reasonably expected to significantly affect the liquidity characteristics of that investment as compared to the fund's other holdings within that asset class.

[6] The rule also would define "convertible to U.S. dollars" to mean "the ability to be sold or disposed of, with the sale or disposition settled in U.S. dollars."

[7] The last sentence of this definition would require funds to classify as "illiquid" those investments that are classified as "level 3" under the US GAAP fair value hierarchy.

[8] Proposal at 60-61.

[9] "For example, in order for a fund to classify an investment as highly liquid on Monday, it would need to reasonably expect that the investment could be sold and settled to U.S. dollars by Wednesday at the latest." Proposal at 68.

[10] A fund must review its classifications "more frequently [than monthly] if changes in relevant market, trading, and investment-specific considerations are reasonably expected to materially affect one or more of its investments' classifications."

[11] Proposal at 75.

[12] The 2016 adopting release for the liquidity rule states, "In our view, if a fund held less than 50% of its assets in highly liquid investments it would be unlikely to qualify as 'primarily' holding assets that are highly liquid investments." Investment Company Liquidity Risk Management Programs, SEC Release Nos. 33- 10233; IC- 32315 (Oct. 13, 2016), at n.726, available at www.sec.gov/rules/final/2016/33-10233.pdf.

[13] Proposal at 79. Moreover, "Consistent with the current rule, a fund would be required to consider a specified set of liquidity risk factors to determine whether its highly liquid investment minimum should be above 10%." Proposal at 80.

[14] The SEC states that this requirement "would not require funds to identify and reclassify specific assets posted as margin or collateral, but rather to reduce the value of the fund's highly liquid assets available to meet the fund's highly liquid investment minimum by the value of the assets posted as margin or collateral." Proposal at 87.

[15] A fund would not be required to specifically identify particular assets that it posted as margin or collateral to cover specific derivatives transactions. Moreover, "This does not mean that the investment acting as margin or collateral would need to be classified as an illiquid investment under the rule. A fund would classify the relevant investment according to the rule's classification framework." Proposal at n.156.

[16] Also, a fund would (i) reduce its reported amount of highly liquid investments by the amount of highly liquid investments that it posts as margin or collateral for derivatives

transactions that are not highly liquid and by the amount of the fund's liabilities; and (ii) increase its reported amount of illiquid investments by the amount of collateral available upon exit of illiquid derivatives transaction.

[17] See Investment Company Liquidity Disclosure, SEC Release No. IC-33142 (June 28, 2018), available at www.sec.gov/rules/final/2018/ic-33142.pdf. The SEC also recently adopted changes to Form N-1A that remove the requirement that a fund briefly discuss the operation and effectiveness of its liquidity risk management program in the shareholder report. See Tailored Shareholder Reports for Mutual Funds and Exchange-Traded Funds; Fee Information in Investment Company Advertisements, SEC Release Nos. 33-11125; 34-96158; IC-34731 (Oct. 26, 2022), available at www.sec.gov/rules/final/2022/33-11125.pdf.

[18] Proposal at 216.

[19] Specifically: (i) references to reasonably anticipated trading size would be replaced with the stressed trade size concept; (ii) information reported about collateral posted as margin or collateral in connection with certain derivatives transactions would be revised; and (iii) information about highly liquid investments would be revised to reflect that not all highly liquid investments will count toward the fund's HLIM.

[20] Specifically, a fund would: (i) name each liquidity service provider; (ii) provide identifying information, including the legal entity identifier and location, for each liquidity service provider; (iii) indicate if the liquidity service provider is affiliated with the fund or its investment adviser; (iv) identify the asset classes for which that liquidity service provider provided classifications; and (v) indicate whether the service provider was hired or terminated during the reporting period.

[21] J.P. Morgan Investment Management Inc., et al., Investment Company Act Release No. 34180 (Jan. 21, 2021).

[22] See proposal at 233 for a list of guidance and no-action letters under review.

[23] Investment Company Swing Pricing, SEC Release No. IC-32316 (Oct. 13, 2016), available at www.sec.gov/rules/final/2016/33-10234.pdf. See ICI Memorandum No. 30333, dated October 21, 2016, for a detailed summary of the 2016 swing pricing amendments.

[24] "Swing pricing" would be defined as "the process of adjusting a fund's current net asset value per share to mitigate dilution of the value of its outstanding redeemable securities as a result of shareholder purchase and redemption activity," pursuant to the rule's requirements.

[25] "Swing factor" would be defined to mean "the amount, expressed as a percentage of the fund's net asset value and determined pursuant to the fund's swing pricing policies and procedures, by which a fund adjusts its net asset value per share."

[26] The "market impact threshold" would be defined as "an amount of net redemptions equal to 1 percent of a fund's net assets, or such smaller amount of net redemptions as the swing pricing administrator determines is appropriate to mitigate dilution." The SEC explains that "[m]arket impact costs reflect price concessions (amounts added to the purchase price or subtracted from the selling price) that are required to find the opposite side of the trade and complete the transaction." Proposal at n.181.

[27] The "inflow swing threshold" would be defined to mean "an amount of net purchases equal to 2 percent of a fund's net assets, or such smaller amount of net purchases as the swing pricing administrator determines is appropriate to mitigate dilution."

[28] The swing pricing administrator would be "the fund's investment adviser, officer, or officers responsible for administering the swing pricing policies and procedures" and may consist of a group of persons. The administration of swing pricing must be reasonably segregated from portfolio management of the fund and may not include portfolio managers.

[29] "Investor flow information" would be defined as "information about the fund investors' daily purchase and redemption activity, which may consist of individual, aggregated, or netted eligible orders, and which excludes any purchases or redemptions that are made in kind and not in cash."

[30] The SEC recognizes that this "spread cost" determination would differ depending on whether a fund values its investments at their "bid" prices or "mid-market" prices when striking its NAVs. "If a fund values its portfolio holdings at the bid price, it would not need to include spread costs in its swing factor when the fund has net redemptions. In contrast, if the fund has net purchases exceeding 2%, the fund would need to include spread costs, which would reflect the full bid-ask spread. For a fund that uses mid-market pricing, it would need to include spread costs in its swing factor any time it applies swing pricing. When a fund using mid-market pricing has net redemptions, or net purchases exceeding 2%, the spread cost component of its swing factor would reflect half of the bid-ask spread." Proposal at 120.

[31] A fund would determine "market impact" by "(A) Establishing a market impact factor for each investment, which is an estimate of the percentage change in the value of the investment if it were purchased or sold, per dollar of the amount of the investment that would be purchased or sold; and (B) Multiplying the market impact factor for each investment by the dollar amount of the investment that would be purchased or sold if the fund purchased or sold a pro rata amount of each investment in its portfolio to invest the net purchases or meet the net redemptions."

[32] The written report would describe: (i) the administrator's review of the adequacy of the fund's swing pricing policies and procedures and the effectiveness of their implementation, including their effectiveness at mitigating dilution; (ii) any material changes to the policies and procedures since the last report; and (iii) the administrator's review and assessment of the fund's swing factors, including the information and data supporting the determination of the swing factors and, if the administrator implements either an inflow swing threshold lower than 2 percent or a market impact threshold lower than 1 percent, the information and data supporting the determination of such threshold.

[33] The fund would maintain its swing pricing policies in effect, or at any time within the past six years were in effect, in an easily accessible place, and written copies of the reports that the administrator provided to the board for six years, the first two in an easily accessible place.

[34] See Items 6(d), 4(b)(2)(ii), 4(b)(2)(iv)(E), and 13(a) of Form N-1A.

[35] "Currently, NSCC is the only registered clearing agency for fund shares, which operates its Fund/SERV service for processing fund transactions." Proposal at 137.

[36] "Eligible order" would be defined to mean "a direction, which is irrevocable as of the next pricing time after receipt, to: (i) Purchase or redeem a specific number of fund shares or an indeterminate number of fund shares of a specific value; or (ii) Purchase the fund's shares using the proceeds of a contemporaneous order to redeem a specific number of shares of another registered investment company (an exchange)."

[37] "Pricing time" would be defined to mean "the time or times of day as of which the investment company calculates the current net asset value of its redeemable securities pursuant to paragraph (a) of this section."

[38] Proposal at 158-200.

[39] The proposal describes this as a separate charge to a transacting investor that would not change the fund's price.

[40] "A fund that uses 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)." Proposal at 172.

[41] "This approach would require that intermediaries (e.g., broker-dealers, banks, and retirement plan recordkeepers) calculate an estimate for what they anticipate the given flows for a particular day to be either before the fund's pricing time or a set time thereafter (e.g., by 4:30 p.m. ET or 5 p.m. ET)." Proposal at 178. Intermediaries then could submit final order flow information after the pricing time once they have received and calculated the final flows for the day.

[42] The proposal explains that funds could generate models that incorporate the information available to them, e.g., the flow information received by a pre-established time as well as historical order flow information in order to estimate expected flows for the day.

[43] The proposal would not change certain nonpublic information currently reported on Form N-PORT, and that information would remain nonpublic (e.g., liquidity classifications for individual portfolio investments).

[44] N-PORT Filers, however, must maintain in their records the information that is required to be included on Form N-PORT not later than 30 days after the end of each month and must produce such records upon request. See General Instruction A to Form N-PORT and Rule 30b1-9 under the Investment Company Act.

[45] The SEC concedes that it could request monthly data from N-PORT Filers but notes that such production would have to be done on an individual basis.

[46] The SEC cites to its prior statements that, before determining whether more frequent public disclosure would benefit investors, it should assess the impact of Form N-PORT data on the mix of information available to the public and the extent to which changes might affect the potential for predatory trading (e.g., front-running or free riding on a fund's research). In support of its proposed changes, it notes that many funds, including actively managed funds, voluntarily provide their complete portfolio holdings monthly on their websites and that ETFs provide transparency daily. In addition, it asserts that "many funds" also provide monthly information about their portfolio holdings to third-party data aggregators (usually with 30- to 90-day lags).

[47] Because the proposal would give investors access to each monthly Form N-PORT filing, information about other months was deemed unnecessary.

[48] This change reflects the proposed requirement that funds would publicly disclose their portfolio holdings on Form N-PORT monthly, rather than only quarterly.

[49] This change aligns with the proposal to make monthly Form N-PORT reports publicly available and would allow the SEC to receive more detailed information about miscellaneous securities holdings.
