Statement on Proposed Amendments to Public Reporting of Fund Liquidity Information

Commissioner Robert J. Jackson, Jr.

March 14, 2018

Thank you, Chairman Clayton, and thank you to the extraordinary Staff in the Division of Investment Management for all of the hard work reflected in this proposal. I appreciate your and the Staff's engagement—and your willingness to answer my questions—a great deal.

Unfortunately, I cannot join the majority in approving this proposal. The Commission today takes the unusual step of re-proposing an already-final, unanimously-approved rule to give mutual-fund investors less, not more, information about the risks that they face. I fear that the result will be to allow large institutions to avoid the costs of a liquidity crunch, leaving Main Street investors holding the bag. For the following three reasons, I respectfully dissent.

First, the proposal exchanges the clear, quantitative data disclosures mandated by the previous rule for qualitative "discuss[ion of] the operation and effectiveness of [the fund's liquidity] program."[1] The reason, the Staff explains, is that quantitative liquidity measures may lack context and reflect fund-by-fund subjective judgments, confusing investors.[2] That may be, but it is hard to see how inviting funds' lawyers to write essays about liquidity will make the information *less* subjective or hard for investors to understand. I hope and expect that the Staff will work diligently to ensure that today's proposal gives investors more than meaningless boilerplate.

Second, the proposal reflects the Staff's concern that disclosure of clear data on fund liquidity could have "pernicious" effects—and, in particular, could lead investors to "flock to more apparently liquid funds, only to discover too late that [the disclosure] did not actually provide comparable liquidity data."[3] But there is little evidence that disclosing liquidity information to investors will cause them to make systematic mistakes of this kind.

So far as I can tell, the only support in the Proposing Release for the conjecture that investors will suffer systematic confusion when faced with quantitative information about liquidity is provided by letters from industry groups.[4] These groups can and should provide their insight to us, but we should not confuse industry arguments with empirical evidence.

Nevertheless, the Staff's concern is worth careful study. That's why I am encouraged that today's proposal requires the Staff to examine the quantitative data that funds will give us privately and report back to the Commission, no later than June 2020, on whether this concern should keep us from providing mutual-fund liquidity data to the public.[5] I look forward to that report and the Staff's insights on that question—and I am grateful for the Commission's willingness to engage with hard evidence in evaluating these complex issues.

Finally—and most importantly—I'm concerned about the potential effects of this proposal for retail investors. Research—and recent experience—makes clear that large institutional investors, unlike their retail counterparts, have a great deal of information about the liquidity of funds like these.[6] Our decision to keep quantitative data on fund liquidity in the dark means that institutional investors—whose position in the market, expertise, and resources give them the ability to detect liquidity issues long before average Americans can—will have a significant informational advantage over retail

investors. If a fund faces trouble, I worry that institutional investors will exit before retail investors know what has hit them—leaving Main Street investors behind in a failing fund.

As our talented Staff has observed, less liquid mutual-fund categories have been growing in recent decades, raising concerns about the ability of those funds to satisfy a fundamental promise of our securities laws: that investors can reliably redeem their shares every day.[7][7] I have no doubt that all of us want to ensure that that promise is kept. I hope that the data the Staff will collect over the coming months will help us better understand the best way to protect retail investors from liquidity risks. And I very much appreciate the hard work reflected in today's proposal.

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[1] SECURITIES AND EXCHANGE COMMISSION, PROPOSED RULE: INVESTMENT COMPANY LIQUIDITY DISCLOSURE (March 14, 2018) [hereinafter Proposing Release], at 15 & text accompanying note 36.

[2] *See, e.g., id.* at 10-13 (describing commenters' view that quantitative data on liquidity can be "subjective," "lack . . . context," and, when provided in isolation, "may encourage investors to focus overly on liquidity risk."

[3] *Id.* at 11 & n.24 (citing Letter from TCW to Chairman Jay Clayton, Commissioner Stein, and Commissioner Piwowar (Sept. 15, 2017)).

[4] *See, e.g.*, Proposing Release at 10 & n. 22 (citing Letter from SIFMA AMG to Chairman Jay Clayton, Commissioner Stein, and Commissioner Piwowar (Sept. 12, 2017)); *id.* at 11 & n.26 (citing Supplemental Comments on Investment Company Liquidity Risk Management Programs from the Investment Company Institute (Nov. 3, 2017)).

[5] *See* Proposing Release at 20 & text accompanying note 48.

[6] For an example in the money-market fund context, *see, e.g.*, PATRICK MCCABE, FEDERAL RESERVE FINANCE AND ECONOMICS DISCUSSION SERIES, FEDERAL RESERVE BOARD, THE CROSS SECTION OF MONEY MARKET RISKS AND FINANCIAL CRISES 15 (2010) ("Compared with their retail counterparts, many institutional MMF shareholders may . . . possess greater sophistication and resources to monitor [fund liquidity] and redeem shares preemptively at the first sign of any heightened risk."). Indeed, our Staff identified similar concerns when we finalized the rule we are modifying today. Securities and Exchange Commission, Final Rule: Investment Company Liquidity Risk Management Programs (October 13, 2016) ("To the extent that economic incentives exist to redeem fund shares prematurely, such redemptions could lead to investor dilution[.]").

[7] Paul Hanouna, Jon Novak, Tim Riley, and Christof Stahel, Securities and Exchange Commission Division of Economic and Risk Analysis, *Liquidity and Flows of U.S. Mutual Funds* (Sept. 2015).