May 18, 2018

Submitted electronically
Secretary Brent J. Fields
U.S. Securities and Exchange Commission
100 F Street, N.E., Washington, D.C. 20549-1090

Re: **File No. S7-04-18**
Proposed Rule: Investment Company Liquidity Disclosure

Dear Secretary Fields,

MSCI appreciates the opportunity to offer these comments to the Securities and Exchange Commission (the "Commission") in response to some amendments to public liquidity-related disclosure requirements and to some amendments to liquidity SEC-reporting requirements proposed in the Commission's recent release entitled *"Investment Company Liquidity Disclosure".* We support the Commission's goals to provide investors with accessible and useful information about a fund's liquidity and to promote effective liquidity risk management practices. We thank the Commission for the opportunity to provide our perspective on the proposed rule.

Background

MSCI is a leading provider of risk management tools, analytical models, data, indexes, real estate benchmarks and ESG research to the world's largest banks, exchanges, hedge funds and asset managers. MSCI is an independent provider with no Asset Management company nor Bank within its corporate structure. MSCI has been actively engaged in liquidity risk management research since 2009 and licenses sophisticated liquidity risk analytics to market participants to support both risk management and regulatory compliance activities (e.g., SEC, UCITS, Form PF). MSCI's views on liquidity risk are the result of a decade long research on the subject, focused on model innovation and regulatory applicability and they have also been informed by the feedback we have received from the asset managers who utilize our liquidity risk management tools.

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Summary

We limit our comments to some of the questions posed in sections II.A.3 “Proposed amendments to liquidity public reporting and disclosure” and II.B.1 “Proposed amendments to liquidity reporting requirements” of the release[1].

Our main observations are:

- We agree that the currently proposed time bucketing is not appropriate for mandatory public disclosure for the inherent level of model risk in its definition.
- We argue that it is still possible to define robust and objective liquidity analytics that could be suited for mandatory public disclosure. We provide some examples.
- We are in favor for a principles-based approach because it would foster diversity of methods, innovation and adaptive evolution to market structure changes.
- We believe that a principles-based approach does not necessarily rule out the adoption of appropriate prescriptive liquidity risk indicators.
- We disagree on the proposal to allow funds to choose between alternative and irreconcilable liquidation bucketing methods under certain circumstances, because this would reduce the utility of the bucketing data reported to the SEC.
- We propose instead to change the definition of the “highly liquid” and “illiquid” buckets in ways that reduce model risk, increase the quality of the reported data and overcome the three circumstances that motivated the current proposal.

Comments to “Proposed amendments to liquidity public reporting and disclosure”

In each of the below comments we specify the corresponding bullet point(s) of section II.A.3, “Comment Request”, pages 21-23, of the release. We have not commented on all bullet points.

- [1st and 2nd bullet points] While we are generally in favor for promoting public transparency about fund liquidity, we agree with the proposal to eliminate the public disclosure of the present version of the time liquidity bucketing classification. The classification involves a high level of model risk (inclusive of several subjective parametric choices from the user of any given risk platform) which does not allow a direct comparison of results obtained from different funds, unless more and more technical information is provided on the nature of the model and on the parameters used to generate the results. Public disclosure may give investors the false

[1] Hereafter we refer to the Federal Register version of the release, available at https://www.sec.gov/rules/proposed/2018/ic-33046.pdf

impression that they can rely on the sole results of the time bucketing for comparing the liquidity of different funds in making their investment decisions.

- [3rd, 10th and 12th bullet point] We do not believe that investors have enough accessible information on fund liquidity yet, but that is not because of the elimination of the time bucketing public disclosure. Other types of information, less prone to model risk, could be considered for required disclosure, such as average fund bid/ask spread, shareholder concentration statistics, and average or stressed holding turnover statistics.

  Also, an improved indicator of promptly available liquidity, expressed in fund NAV percentage, similar to the existing "highly liquid" time bucket, could achieve appropriate standards for mandatory public disclosure purposes, if redesigned so as to reduce model risk and remove altogether any subjective inputs.

  a. For example, one could define the "highly liquid portion" of a fund as the NAV fraction of all positions (or fractions of positions) that can be traded in one day and settled within three days at transaction costs not exceeding the position's half bid/ask spread augmented by a fixed prescribed tolerance, say 20%. Notice that this is in the same logic as a "proportional" liquidation bucketing, because contributions may also come from fractions of positions: in this way, one avoids the introduction of a subjective notion of "portions that the fund would reasonably anticipate trading".

- [7th and 9th bullet point] We believe that a narrative description of the operation and effectiveness of liquidity risk management programs can be useful if written in terms that are accessible to broad investors, together with – but not in alternative to – a description of noteworthy specific events that occurred during the period in question (such as the adoption of some liquidity management tools), as well as relevant changes to the liquidity risk management program.

- [13th bullet point] We support the promotion of principles-based approaches to liquidity risk management as suggested by the Treasury[2] and in line with international guidelines recently set forth by IOSCO[3]. We believe, however, that such an approach does not need to exclude complementary prescriptive requirement and possibly disclosure of select liquidity indicators with good standards of objectivity and comparability, as described in our previous comments.

  We believe that a principles-based approach would promote innovation in liquidity risk management and allow funds to adopt different methodologies available for specific strategies and asset classes. For the enforcement of a principles-based approach, the role of regulators

[2] https://www.treasury.gov/press-center/press-releases/Documents/A-Financial-System-That-Creates-Economic-Opportunities-Asset_Management-Insurance.pdf

[3] http://www.iosco.org/library/pubdocs/pdf/IOSCOPD590.pdf

would be to set forth the principles, to control their observance and to promote the adoption of best observed practices among peers.

A list of reasons in favor for a principles-based approach includes:

a) Different liquidity risk management practices and liquidity metrics are applicable by funds with different strategies, typically because of heterogeneous data availability across asset classes. A principles-based approach allows funds to adopt the best possible methods available to them, as opposed to any prescribed one-size-fits-all approach.

b) Evolution and progress in liquidity risk management is still largely under way. A principles-based approach promotes innovation from multiple voices and reduces the risk of monoculture.

c) It's hard to condense the complexity of liquidity risk in a finite number of one-size-fits-all indicators. A principles-based approach gives funds a way to provide complementary views of their liquidity to any set of prescribed metrics.

d) The continuous evolution of markets structure may make any prescriptive rule obsolete in a short time. A principles-based approach gives funds a way to react more promptly to a fast-changing market environment. Increasing bond market transparency, for instance, will make new types of data available and permit more sophisticated liquidity measures.

e) A principles-based approach promotes harmonization of practices across jurisdictions even when jurisdiction-specific constraints exist for the adoption of liquidity management tools.

Comments to "Proposed amendments to liquidity reporting requirements"

In each of the below comments we specify the corresponding bullet point(s) of section II.B.1, "Multiple Classification Categories", pages 26-27, of the release. We have not commented on all bullet points.

- [1st bullet point] We believe that a "proportional" liquidation bucketing, possibly mapping a position into multiple buckets according to a sequential liquidation of a position's tranches is more meaningful for the determination of a fund highly liquid component (assets that trade in one day and settle in 3 days) than the one-to-one assignment of positions to single buckets. The latter may be more appropriate for the determination of the 15% illiquid assets (assets that require more than 7 days just to be traded) which are usually characterized by specific size-independent asset properties rather than market depth or capacity.

We see, however, several potential problems with the current proposal to allow funds to split holdings among different categories only in certain circumstances:

a) The proposal would open the possibility for different funds to adopt different bucketing schemes. However, the two bucketing schemes yield irreconcilable results. The proposal would therefore reduce the utility of the entire bucketing exercise because the data collected by the SEC would not permit industry-wide comparisons and surveys.

b) The proposal is motivated as an ad hoc workaround to three categories of possible practical problems and not as an attempt to improve the quality of the reported information for all funds.

c) We do not understand the motivation behind the first circumstance. If different portions of a holding possess contractual differences leading to different liquidity properties, then they should be represented as different holdings. If, on the other hand, a holding (say a bond) is hedged only in part by a derivative (say a swap), what would be helpful is the possibility to classify hedged positions (here the resulting "asset swap") as a whole, within a comprehensive set of rules for the treatment of derivatives, rather than just the splitting of the holding into multiple buckets.

d) In the second circumstance mentioned in the proposal (multiple sub-advisers managing different sub-portfolios with common assets), the split classification of a holding, possibly in two non-adjacent buckets, would just signal an inconsistency between different sub-advisors' models and would not provide any useful information.

For the above reasons, as an alternative to the Commission's proposal, we would suggest changing the definition of the current "highly liquid" and "illiquid" buckets[4], which are the two buckets subject to limits, with the following reporting requirement for all funds:

I. The "highly liquid portion" of the fund, subject to "highly liquid investment minimum", as described in the previous section, based on the "proportional" liquidation of all holdings, including contributions from both entire positions and fractions thereof.

   a. The proposal should be accompanied by a comprehensive set of guidelines for the treatment of derivatives holdings.

II. The "illiquid portion" of the fund, subject to "15% illiquid investment limit" including only contributions from entire positions, characterized by the latency of their marketability.

[4] We do not have any specific proposal for the "moderately liquid" and "less liquid" buckets which we consider less important and inherently affected by higher model risk.

We note that this alternative proposal:

  - Would improve the quality of the reported information
  - Would require all funds to report the same type of information
  - Would lower model risk and eliminate subjective inputs
  - Would solve at once the issues in the three circumstances mentioned in the current proposal

- [2nd and 5th bullet point] Within the current proposal we believe that whatever liquidation scheme a fund may adopt, it should be consistently used across its holdings, or the resulting bucketing would be completely meaningless. Our answers to the 2nd and 5th bullet points are therefore yes and no, respectively.

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Thank you again for the opportunity to comment on the Commission's proposals. If you have any questions about MSCI's comments or would like additional information, please contact us.

Sincerely,

/s/ Carlo Acerbi

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