State Street Corporation
One Congress Street
Boston, MA 02114-2016

statestreet.com

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International Organization of Securities Commissions
Calle Oquendo 12
28006 Madrid
Spain

Submitted via: online survey

Re: IOSCO Consultation Report on ""Revised Recommendations for Liquidity Risk Management for Collective Investment Schemes"

Questions for consultation

1. **Are the identified common components of OEF's structure including notice periods, lock-up periods, settlement periods and redemption caps accurately described? Are there any relevant additional considerations when setting the notice periods, lock-up periods, settlement periods or redemption caps?**

State Street has over the past years welcomed and supported the work by the International Organization of Securities Commissions ("IOSCO") and the Financial Stability Board ("FSB") focusing on sound risk management practices, particularly with a view to address liquidity mismatch and first mover advantage risks for certain investors in open-ended funds ("OEFs").

In supporting this work, State Street has promoted a principles-based approach acknowledging that open-ended funds vary significantly in their portfolio investments and liabilities, investment strategies, investor flows and shareholder bases, elements that need to be recognized when setting policy and liquidity requirements.

In this vein, State Street welcomes the approach taken by IOSCO which explicitly integrates the following important principles:

- depending on local conditions and circumstances, the implementation of the revised Recommendations may vary from jurisdiction to jurisdiction;
- the exclusion from the scope of the revised Recommendations of ETFs and MMFs which have structural characteristics setting them apart from other OEFs;
- that Fund Managers retain the primary responsibility to manage liquidity in their OEFs and that there is no one-size fits all approach to managing liquidity risk.

With these principles in mind, we broadly support the spirit of Recommendation 3 and the principle that responsible entities should give due consideration to the fund structure, its liquidity profile and dealing frequency. However, we would like to share some considerations as regards the way that the assessment of asset/portfolio liquidity is presented and on the way the categorization approach for OEFs will be operationalized.

There is no widely or industry-accepted approach to quantifying asset liquidity, whether in normal or stressed market conditions. The multi-faceted aspect of liquidity, including expected or assumed trading size, may lead to different outcomes across funds of similar size, assets and strategy. Judgments about asset liquidity are always based on observations and estimates, and the liquidity profile of a fund is always dynamic, with liquidity needs that need to be assessed on an ongoing basis.

Therefore, we do not support top-down categorization of OEFs and when implementing this Recommendation we urge caution not to over-engineer the assessment and classification of liquidity into an overly prescriptive framework, which may not be realistic due to market dynamics and changes in the factors that drive liquidity.

In the explanatory text to Recommendation 3 IOSCO rightly notes that the categorization approach should be aligned with domestic liquidity frameworks and always take into consideration the entirety of a OEF's portfolio and not looking only at a subset of assets. However, in setting forward arbitrary thresholds for less liquid and illiquid assets the risk is instead to overly simplify the assessment of a fund's liquidity while implicitly introducing cliff edge risks in moving from one category to the other. Creating rigidity in the framework of liquidity management, through thresholds or otherwise, could lead to unintended risks and costs, especially if the regulatory approach is dependent on measurements of liquidity that are not widely accepted or adopted.

We remain supportive of more targeted means of addressing liquidity mismatch in illiquid funds (for example via reduced redemptions terms, Liquidity Management Tools ("LMTs") or more structural features such as notice periods, lock-up periods, settlement periods or redemption caps) but this determination should be made at the fund's inception through product design and through appropriate and sophisticated liquidity risk metrics not through a prescriptive categorisation approach.

At State Street, the primary risk metric for our open-end funds is Liquidity Coverage Ratio ("LCR"), estimated for both normal and stressed market conditions and used to monitor mismatch between fund's assets and liabilities on an ex-ante basis. LCR measures if the fund has adequate sources of liquidity (liquid assets that can be converted into cash) which are sufficient to cover liquidity needs (redemptions) under normal or stressed market environment. In addition, Estimated Liquidation Cost / Market Impact, Time to Liquidate, Bid-Ask Spreads, % of the fund invested in securities with certain liquidity risk characteristics (market cap, issue size, traded volume, time to liquidate, etc.), and Investor Concentration Index (HHI) are all supplemental metrics included as part of Liquidity Risk Management framework. This sophisticated liquidity risk analysis cannot be reduced to a categorization approach.

To conclude, we reiterate our support for a differentiated regional regulatory approach as opposed to a one-size fits-all approach globally, and we consider that Recommendation 3 should apply on a principles-basis, allowing jurisdictions to use equivalent approaches to the categorisation, such as for example the stress testing framework in place in Europe.

2. **Are there any other key considerations related to the availability and use of anti-dilution LMTs, quantity-based LMTs and other liquidity management measures under normal and stressed market conditions?**

We broadly concur with Recommendation 6 and we have in the past consistently supported, in accordance with jurisdictional specificities, expanding the availability and use of LMTs and anti-dilution tools.

As general principles, we consider that investment managers, in pursuing their fiduciary duty, remain best placed to activate and calibrate these tools on the basis of their fund's investment strategy and portfolio liquidity. Moreover, in deploying anti-dilution and quantity-based LMTs, the focus should remain on material dilution risks while the inclusion of implicit transaction costs should remain on a best effort basis, provided that the trade sizes of the fund are large enough to result in a market impact. Because implicit transaction costs are difficult to estimate (especially due to inconsistency of market impact data) we struggle to see how the inclusion of these implicit costs will be able to drive consistency among open-ended funds, and therefore the best interest of investors.

We would also like to stress the importance of IOSCO's comment that while responsible entities may set up activation thresholds for a particular LMT, activation should always remain at discretion of the fund manager and never be automatic. An automatic activation would not allow for proper consideration of the specific circumstances that exists at each point in time, or whether the activation of the LMT is in the interest of investors.

At State Street, strong liquidity management has always been part of our fiduciary duty and we have a wide range of recognized tools/best practices in place to manage fund liquidity and redemptions. This includes tools for managing day-to-day liquidity, as well as tools to cope with more extreme tail risk events and first-mover advantage risks. These tools range from ongoing monitoring of asset liquidity compared to expected redemptions, to more proactive measures in times of financial stress, such as swing pricing, redemption fees and gates. Not all such tools are necessary or appropriate in all markets, or for all fund types, nor is dilution always a material risk, and fund managers are able to assess this with the help of their liquidity management playbooks.

Swing pricing in particular has been widely deployed across our EU and UK-registered funds in recent years, both for subscribing as well as redeeming investors. The swing pricing framework in Europe remains optional and leaves funds with the ability to set their own swing factors and thresholds (with no mandatory inclusion of market impact in swing factors). This experience is however not instructive for the U.S. marketplace given the differences in the shareholder base, fund operating models and fund distribution infrastructure.

3. **Are there any other LMTs or liquidity management measures commonly used by OEF managers?**

We believe that the Recommendations have correctly identified the most common LMTs but we would suggest that any list is not made exhaustive but leaves space for future evolutions in market practice.

4. **Have the proposed changes covered all the essential elements regarding liquidity risk management governance arrangements in relation to the use of liquidity management tools and other liquidity management measures? Are they proportionate to the differing size and complexity of responsible entities' fund ranges?**

State Street agrees that effective governance arrangements are crucial for the deployment of liquidity and anti-dilution tools, and that this process should be integrated into wider fund governance. We believe that the explanatory text to Recommendation 13 captures all the key elements that should be included in a sensible governance process around liquidity management.

Current market practice should already be integrating all these elements into funds' liquidity Playbooks, outlining information about available risk mitigants and decision-making processes relevant to each fund range. The appropriate structure will vary depending on fund type and jurisdiction and we would discourage any recommendations or prescriptive guidance which would prescribe specific models or factors to be taken into account in the design and calculation of anti-dilution tools, which would result in a limitation of the judgement of Funds Managers to act in the best interest of investors. The governance process should integrate adequate flexibility and discretion to respond to all possible future market events.

The one note of caution that we would stress is that any thresholds for activating LMTs should not in any circumstance require a mechanical or automatic activation, but should rather act as a trigger for the fund Manager/fund Board to consider whether to activate a particular LMT based on the specific set of circumstances and on the best interest of investors.

As regards the role of depositories and third parties, we would like to note that depositories are generally already required in many jurisdictions to conduct a regular and comprehensive oversight of a fund's compliance with liquidity risk management processes, including procedures around LMTs, and to oversee the calculation of units and share dealing. However, they are not and should not be required to assess the adequacy of selected liquidity risk metrics nor the outcome of the valuation of units, which should remain responsibility of the fund Manager/Board.

5. **Please describe any material factors of the liquidity risk management governance and oversight arrangements which have not been included.**

Please refer to our previous response.

6. **What information can (and should) be disclosed to investors or the public, and within what timeframe should this information be disclosed to enhance transparency when responsible entities activate quantity-based LMTs or other liquidity management measures?**

State Street agrees that investors should receive appropriate disclosure concerning which LMTs and anti-dilution tools have been selected, including a description of their nature and the fact that the fund Manager/fund Board can utilize them. In the prospectus, funds are able to clearly disclose the presence and possible use of LMTs. This should allow investors to take the associated cost of liquidity into account in their investment decisions, without the need to disclose details about calculation methodologies, triggers or details about the circumstances of invocation of each LMT.

In fact, we would caution against including every scenario or condition for activation/ deactivation and instead focus at a high level the conditions that each manager may consider when applying an LMT. We appreciate that IOSCO recognizes that an appropriate balance needs to be struck to avoid unintended consequences and counterproductive behaviors by sophisticated investors. We would also urge against needing to disclose the governance behind the activation/ deactivation outside of noting who the decision sits with – i.e. the Board, the Investment Manager or the Manager.

7. **Do you have any comments on any of the other Proposed Revised Liquidity Recommendations put forth in this document?**

No further comments.