Dreyfus

THE DREYFUS CORPORATION

January 10, 2011

VIA EMAIL TO RULE-COMMENTS@SEC.GOV

Ms. Elizabeth Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

RE: President's Working Group Report on Money Market Fund Reform
File No. 4-619; Release No. IC-29497

Dear Ms. Murphy:

The Dreyfus Corporation ("Dreyfus") welcomes the opportunity to comment on the money market fund reform options (the "Policy Options") discussed in the "Report of the President's Working Group ("PWG") on Financial Markets" (the "Report"). Dreyfus is registered with the U.S. Securities and Exchange Commission (the "Commission") as an investment adviser under the Investment Advisers Act of 1940. Dreyfus manages approximately $405 billion in assets, including approximately $287 billion invested in over 190 investment company portfolios, of which approximately $205 billion is invested in 49 domestic money market mutual funds structured within the confines of Rule 2a-7 under the Investment Company Act of 1940. Dreyfus is a subsidiary of BNY Mellon, a global financial services provider with over $1.1 trillion in assets under management and over $24 trillion under administration and custody.

We commend the PWG's fair and balanced consideration of the potential for each Policy Option to reduce money market funds' susceptibility to runs. We were particularly pleased that the PWG was guided by a concern for mitigating possible adverse consequences of further regulatory change, such as the potential flight of assets from money market funds to less regulated or unregulated vehicles, and that the PWG recognized potentially effective Policy Options for reducing systemic risk without requiring the extreme act of transitioning to a floating net asset value ("NAV") for money market funds.

We offer the following summary comments, which are more fully discussed below.

Comment Summary.

1. We believe first and foremost that it is unnecessary to obsolete Rule 2a-7, stable NAV money market funds in order to reduce systemic risk. Accordingly, we do not support the Policy Option of adopting a floating NAV for money market funds, which we believe would be problematic to implement, and which poses other significant negative consequences.

2. Among the other Policy Options discussed in the Report, we believe a private emergency liquidity facility (the "Private Liquidity Facility") is the one Policy Option that would effectively reduce money market funds' susceptibility to runs and enhance their ability to withstand runs. To that end, we support the current industry initiative to develop a model for a Private Liquidity Facility that would serve as a liquidity back-stop for prime money market funds during times of unusual market stress.

3. Correspondingly, we believe the remaining Policy Options, some of which also present significant negative consequences, ultimately would not reduce systemic risk.

These comments are discussed more fully below.

Discussion.

1. We do not support eliminating stable NAV money market funds.

We believe the Report has accurately identified the reasons why transitioning from a stable NAV to a floating NAV for money market funds may not mitigate systemic risk. First, we agree that this Policy Option could not be implemented without causing systemic stress to the financial markets and to the economy. There is no one, practical solution for implementing this change that would not be systemically disruptive to the markets and the economy. Secondly, we believe a floating NAV would reduce systemic risk only nominally, because floating NAV investments that would continue to be used for ready liquidity would still be subject to runs as those investors seek to "get out first" in order to minimize losses. Thirdly, we believe that if the Commission were to mandate a floating NAV it would eliminate the liquidity vehicle of choice for millions of retail and institutional investors while only shifting systemic risk to those liquidity vehicles that would replace the stable NAV money market fund.

We strongly agree with the statement in the Report that the transition from a stable NAV to a floating NAV itself would be systemically risky, because we believe that implementing this Policy Option would precipitate the movement of at least hundreds of billions of dollars to alternative (regulated or unregulated) liquidity sources. Conversely, we strongly disagree with the following statements in the Report which are offered as a justification for moving to a floating NAV:

> *"…..making gains and losses a regular occurrence, as they are in other mutual funds….could alter investor expectations and [make them] more accustomed to and tolerant of NAV fluctuations and less prone to sudden, destabilizing reactions."*
>
> *"investors would have less of an incentive to run from money market funds with floating NAVs than from those with stable, rounded NAVs."*

Liquidity investing, by its very nature, is loss-averse. Moving to a floating NAV will not change the nature of liquidity investing – it will only relocate it to different vehicles, where the same intolerance for loss will be evidenced during periods of unusual market stress that threaten the stability of liquidity balances broadly. In an environment where floating NAV funds have replaced stable NAV funds, we believe floating NAV funds also would be likely to experience *"sudden, destabilizing reactions"* during periods of unusual market stress. While the "investor left behind" in a stable NAV fund likely faces a loss of about 1% (before the fund liquidates and winds up its affairs), a floating NAV fund also can have "investors left behind" who can be subject to deeper downside market value risk with a small likelihood that those losses could be recovered through capital gains. Faced with that risk, substantial net redemption activity during periods of unusual market stress would be foreseeable in floating NAV funds.

In part, our opinions are based on feedback from our fund shareholders. For example, as noted in our comment letter to the Commission in September 2009 on the proposed amendments to Rule 2a-7 (the "2a-7 Comment Letter"), we surveyed 37 of the largest Dreyfus institutional money market fund shareholders (with over $60 billion invested) and asked them, inter alia, whether their respective businesses could continue to utilize a money market fund for short-term liquidity needs if a floating NAV was introduced. We reported that two-thirds of these shareholders said they would seek an alternative liquidity investment. Of these respondents, 50% said they could not tolerate the principal risk associated with a floating NAV, 16% cited systems support obstacles (mainly, cash sweep accounts), and 8% cited relevant investment guidelines that would prohibit that transaction.[1]

We believe these results support the view that floating NAV money market funds would not serve the liquidity needs of investors, and that moving to a floating NAV would precipitate the prompt transfer billions of dollars from stable NAV money market funds to other liquidity vehicles that do not have the protections afforded by Rule 2a-7,[2] which itself would have significant systemic implications. Further, we refer to the statement in the Report that *"there is no direct evidence on the likely effect of a floating NAV on the demand for money market funds"* and suggest that our survey offer relevant "direct evidence" that the demand for money market funds would be substantially lower if a floating NAV replaced the stable NAV.

We also disagree with the suggestion in the Report that moving to a floating NAV is advisable in order to dispel investor expectations that money market funds are "risk-free cash equivalents" and make them less systemically vulnerable. We do not believe that investors, particularly institutional investors, believe that money market funds are risk-free investments. To the contrary, institutional investors have increased their demand for due diligence meetings and have demonstrated greater vigilance about portfolio holdings and strategies (among other aspects of money fund investing). We believe this behavior evidences a strong appreciation for the risk of loss inherent in stable NAV money market fund investments and, like investors past net redemption activity during periods of unusual market stress, is inconsistent with the belief that their investment is "risk-free."

Similarly, the Report also suggests that past sponsor support has lent credence to the expectation that stable NAV money market funds are risk-free investments, but sponsors in the past also have taken actions to remedy credit issues in unregistered liquidity portfolios and there is no guarantee that they would not continue to do so to support floating NAV money market funds. Thus, we do not believe that past sponsor support is a factor unique to stable NAV funds or that necessarily favors transitioning from a stable NAV to a floating NAV.

2. **We support the industry-sponsored undertaking to establish a model for a Private Liquidity Facility that would serve as a back-up source of liquidity for prime money market funds during times of unusual market stress, such as when the fixed income markets are not providing appropriate pricing mechanisms for, or buyers of, portfolio securities due to the severe market illiquidity.**

Following the failure of Lehman and then Reserve Primary Fund, many "prime" money market funds struggled to withstand the substantial redemption requests that ensued, because they were unable to sell certain privately issued portfolio securities into a liquid market that would have provided appropriate pricing. As the stress on money market funds began, the U.S. Treasury Department's Temporary Guarantee Program for Money Market Funds (the "Guarantee Program") provided some immediate, short-term calm, but ultimately it was not the mechanism for investors to maintain confidence in prime money market funds during this period. Rather, the temporary facilities that were established by the Federal Reserve (e.g., the Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility), which provided immediate, ready liquidity to the commercial paper and asset-backed securities markets, were the critical factor in maintaining the viability of prime money market funds. This was because the Guarantee Program did not guarantee shares acquired after the September 19, 2008 effective date of the Program in excess of the amount held in an account on that date.

Conversely, a Private Liquidity Facility offers the money market fund industry an equivalent solution to the temporary facilities that were established by the Federal Reserve and logically should also materially assist in stemming runs on prime money market funds precipitated by market illiquidity. Without these temporary facilities operating until market liquidity conditions normalized, prime money market funds would have been unable to attract new investments, and instead would have experienced a steady drain on assets that still would have threatened their continued existence.

We believe the Report appropriately directs policymakers to *"aim primarily at mitigating systemic risk and containing the contagion effect that strains at individual money market funds can have on other money market funds and on the broad financial system,"* and we believe a Private Liquidity Facility offers a tangible, effective means for prime money market funds to limit the contagion effects of a Lehman or a Reserve-type failure and to manage through a liquidity crisis, even one of the magnitude of 2008. The Report also characterizes as *"imperative"* the need for the money market fund industry to *"internalize fully the costs of liquidity or other risks associated with their operation"* in order to *"forestall"* the likelihood that money market fund investors would continue to expect government support at minimal cost to remedy another crisis. We also see a Private Liquidity Facility as answering that call.

Currently, we are participating with the Investment Company Institute ("ICI") and other money fund providers to develop a suitable model for a Private Liquidity Facility that would serve as a back-up for prime money market funds, when the fixed income markets are not functioning correctly and liquidity dries up. We recognize the several issues associated with establishing a Private Liquidity Facility, including:

- adequately capitalizing the Facility to provide for its effective operation in an environment like the kind experienced in 2008[3];
- regulatory issues related to establishing the Facility;
- the scope of money market funds' participation; and
- governance and financial management of the Facility

In this regard, we refer the Commission to the presentation made in ICI's comment letter on the Report regarding the development of a model for a Private Liquidity Facility. We think it is a viable proposal capable of being adequately capitalized over time to the extent required to support prime money market funds en masse, and we will continue to work with ICI and other money fund providers to make the Private Liquidity Facility a viable concern available to stable NAV prime money market funds.

We do not believe that challenge to adequately capitalize a Private Liquidity Facility in the short-term should marginalize the value it offers to meaningfully reduce systemic risk. In this regard, we note that Dreyfus also is represented on the Asset Management Group ("AMG") of the Securities Industry and Financial Markets Association, and we refer you to the discussion in the AMG's comment letter on the Report that discusses the issues associated with a Private Liquidity Facility and the reasonableness behind the time required to capitalize it appropriately, for the benefit of stable NAV money market funds and their shareholders.

The Report also states that *"a private emergency facility could play an important role in supplementing the SEC's new liquidity requirements for money market funds"* and that such a facility *"should be the subject of further analysis and discussion."* We agree with this conclusion and recommendation. We believe an adequately capitalized Private Liquidity Facility, when coupled with the Daily, Weekly, and General

Liquidity Standards currently provided for under Rule 2a-7, would substantially reduce the systemic risk associated with stable NAV, prime money market funds. Collectively, these Standards and the Private Liquidity Facility would appear to offer a strong and effective solution to the circumstances that arose in 2008 if they were to reoccur.

3. **We believe the remaining Policy Options, some of which pose potential adverse consequences, ultimately would be unsuccessful in mitigating systemic risk, particularly during a liquidity crisis.**

Because we believe the Private Liquidity Facility is the only reasonable Policy Option that would reduce systemic risk, we do not believe that an extensive exposition regarding the remaining Policy Options is necessary, so instead we offer the following additional comments on certain of the Policy Options that we believe are most important for Commission consideration.

Mandatory In-Kind Redemptions. As stated in our 2a-7 Comment Letter, we continue to oppose the Policy Option of requiring large redemptions to be satisfied in-kind, due to the associated portfolio disruption and shareholder servicing issues, and we disagree with the assertion made in the Report that in-kind redemptions for large investments would reduce the incentive to redeem. To the contrary, Institutional investors (i.e., the class of investors most likely to have such "large" redemptions) would look unfavorably on the prospect of receiving their redemption proceeds "in-kind" (particularly, in respect of large balances), because the delivery of portfolio securities is inconsistent with the ready liquidity they require. Thus, we believe large institutional investors with large investment amounts likely would eschew money market funds altogether or, when faced with the reasonable likelihood of receiving redemption proceeds in-kind, would precipitate a run on a fund in order to receive cash instead of securities. In-kind transactions also would impose complex pricing, valuation, cost, and operational issues on both the fund and on investors who receive them.

Moreover, we believe prudent fund management requires that the fund's adviser retain the flexibility to determine whether delivering redemption proceeds in cash or in-kind is in the best interest of all fund shareholders. The adviser must retain this flexibility in order to most effectively discharge its fiduciary responsibility to all shareholders in a fund.

Insurance. We agree that a private insurance program most likely is cost prohibitive. Further, and contrary to the analogy made in the Report, we do not agree that a private insurance program would have a similar impact as the Guarantee Program or that the Guarantee Program was "akin to deposit insurance." The Guarantee Program was for a limited term and only "guaranteed" shares up to the maximum number held in an account as of a specific date (September 19, 2008), and while it contributed to stemming the tide of redemptions near-term, investors did not reasonably analogize it to deposit insurance because it did not provide a guarantee for shares subsequently acquired that increased account balances over the investor's September 19th balance. Further, the Guarantee Program provided guarantees without regard to the total number of shares owned in an account on September 19th, which amount could have been in the billions, and thus we question the appetite for insuring balances of such size from a competitive perspective. Overall, we do not believe that the success of the Guarantee Program provides a viable example for the potential effectiveness of a private insurance program.

"Two-Tiered" Regulatory System. For the reasons cited above that explain our views on a floating NAV money market fund, and the current lack of demand for existing, floating NAV, "Rule 2a-7-like" money market funds, we cannot see how a two-tiered system would reduce systemic risk. While in principal we generally would not oppose Rule 2a-7 accommodating a type of floating NAV money market fund along with the stable NAV money market funds as currently constructed, we disagree that providing this "flexibility" would reduce systemic risk, because we believe liquidity would continue to be housed almost exclusively in stable NAV money market funds.

Similarly, as noted in the Report, and for many of the same reasons already stated above, we do not support the Policy Option of preserving the stable NAV money market fund only for "retail" investors, because we agree with the assertion in the Report that the *"consequences"* of such a dual structure for retail (stable NAV) and institutional (floating NAV) money market funds (even if the definitional challenges raised during the comment period for the proposed Rule 2a-7 amendments were resolved to the industry's satisfaction) would be *"no different"* than eliminating the stable NAV altogether.

Once again, we thank the Commission for the opportunity to present our views on these important issues. If you have any questions or require additional information from me, please do not hesitate to contact me at (212) 922-8109. Also, you may wish to contact John B. Hammalian, Managing Counsel, at (212) 922-6794 or at hammalian.j@dreyfus.com.

Sincerely,

J. Charles Cardona

J Charles Cardona
President
The Dreyfus Corporation

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[1] We also asked these investors *"What role does safety of principal and a stable NAV play in your investment decision to utilize a money market fund?"*; and 86% responded that a stable NAV was "very important" to their investment decision. Several of these respondents noted that operational issues associated with floating NAVs would virtually eliminate the money market fund as an eligible option for sweeping cash assets. We further asked *"Would you view a floating NAV money market fund as 'more risky'?"* and 83% of those surveyed indicated that they would consider a floating NAV money market fund "more risky." Responses also indicated that a floating NAV would require a greater amount of due diligence inquiry to explain price variations, the burden of which, we believe, would cause some money fund providers to exit the business.

[2] In our survey, many clients indicated that floating NAV products are in the market today, but that they do not use them because they do not provide the same flexibility or liquidity that stable NAV money market funds offer. Other clients indicated that they have found some use for floating NAV products, but only to support their demand for direct investment in a longer duration product. These clients further indicated that floating NAV products are not their product of choice for operating or excess cash needs, which require same-day liquidity without capital gain/loss issues. They also indicated that floating NAV money market funds would be difficult to differentiate from other types of short-term mutual funds, which would possibly add confusion to their investment their investment selection process.

[3] In this regard, we note that other Policy Options might entail bank-like capital commitments by money market funds and/or money market fund providers. For a variety of reasons, we do not support bank-like capital requirements for money market funds, and we refer you to the comments provided by SIFMA's AMG in this regard in its comment letter to the Commission, which we support. Correspondingly, we do not equate capitalization of the Private Liquidity Facility with imposing a bank-like capital requirement.