MEMORANDUM

TO: File

FROM: Sarah G. ten Siethoff
Senior Special Counsel
Division of Investment Management

DATE: March 22, 2013

RE: Money Market Fund Regulation and Special Study on Money Market Funds

On March 18, 2013, Diane Blizzard and Sarah ten Siethoff from the Division of Investment Management ("IM") met with the following representatives from Fidelity: Nancy Prior, Kevin Meagher, and James Febeo, Jr..

Among other matters, the meeting participants discussed money market fund reform options and the analysis contained in the November 30, 2012 special staff study on money market funds prepared by the Division of Risk, Strategy and Financial Innovation.

Money Market Mutual Fund Reform Update

March 18, 2013

Impact of SEC 2010 Amendments to 2a-7

- **2010 reforms significantly improved overall soundness of MMFs and made them more resilient to market stress**
  - Stringent constraints on portfolio liquidity, maturity and quality
  - New disclosure, operations, risk and governance requirements
- **MMFs now required to hold approximately $800 billion in liquid assets**
  - Actual liquidity levels in funds today are well above the required level
- **2010 reforms were proven effective during the summer of 2011**
  - Key market events: European debt crisis, U.S. debt ceiling showdown, S&P downgrade of U.S. credit rating
  - More than $170 billion flowed out of MMFs in an 8-week period, yet investors were able to redeem their money, sometimes up to 30% of a fund's total assets, without issue

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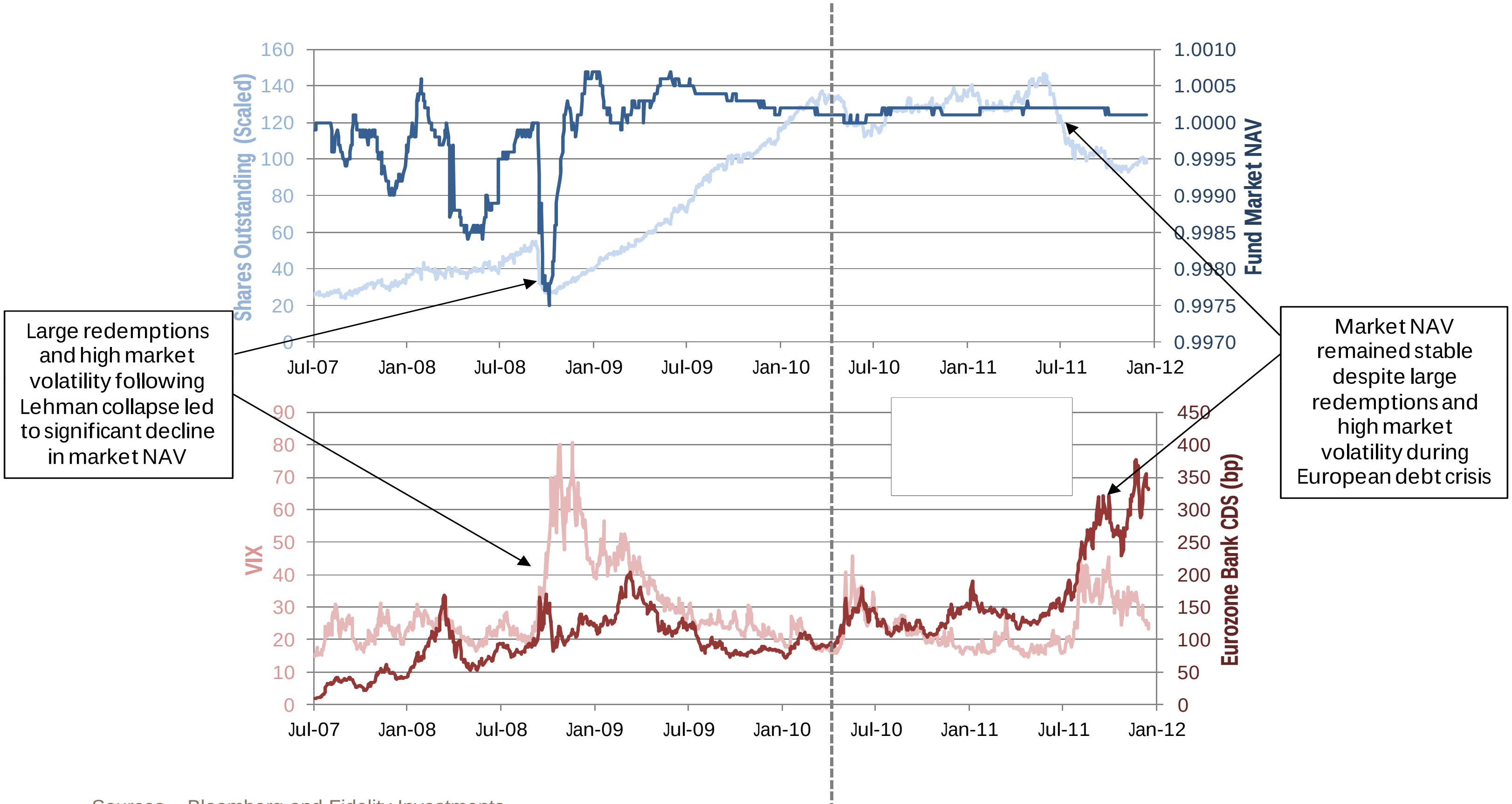
Impact of 2011 Market Turmoil on U.S. MMFs

» **Following the 2010 reforms, the market NAV of a representative prime fund has remained remarkably stable despite periods of heavy redemptions and high market volatility**



Sources – Bloomberg and Fidelity Investments

FSOC Proposals

- **Alternative 1: Floating NAV**
  - All types of funds are included – Treasury / Government / Municipal and General Purpose
- **Alternative 2: Stable NAV with capital and redemption restrictions**
  - Capital buffer of 1%
  - Minimum balance at risk (MBR) – Holdback 3% of a shareholder's highest account value in excess of $100,000 during the previous 30 day period
- **Alternative 3: Stable NAV with higher capital requirement and "other measures"**
  - Capital buffer of 3%
  - May reduce buffer amount by implementing other measures such as greater diversification, increased liquidity, and/or more frequent holdings disclosure
- ***FSOC's proposed recommendations are not workable – they would cause significant redemptions from MMFs, disrupt the financial marketplace, and increase systemic risk***

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FSOC Comment Letter Summary

- **132 responses were submitted responding to the FSOC's Proposed Recommendations from a wide range of market participants**
  - Federal Reserve Regional Bank Presidents
  - Former Chairmen, Commissioners and Senior Staff of the SEC
  - State / Local Governments – Treasurers, Mayors, Chambers of Commerce
  - Money Market Advisers / Asset Managers
  - Trade Associations and Advocacy Groups

- **Of the letters that addressed the FSOC's recommendations, an overwhelming majority opposed all three options**
  - Alternative 1 - Floating NAV: ***83% opposed***
  - Alternative 2 - 1% Capital / MBR: ***91% opposed***
  - Alternative 3 - 3% Capital: ***82% opposed***

- **Emerging consensus that Treasury, Government and Municipal funds should be excluded from further reform (based on letters that addressed issue)**
  - Treasury funds: ***95% support*** excluding from further reform
  - Government funds: ***88% support*** excluding from further reform
  - Municipal funds: ***84% support*** excluding from further reform

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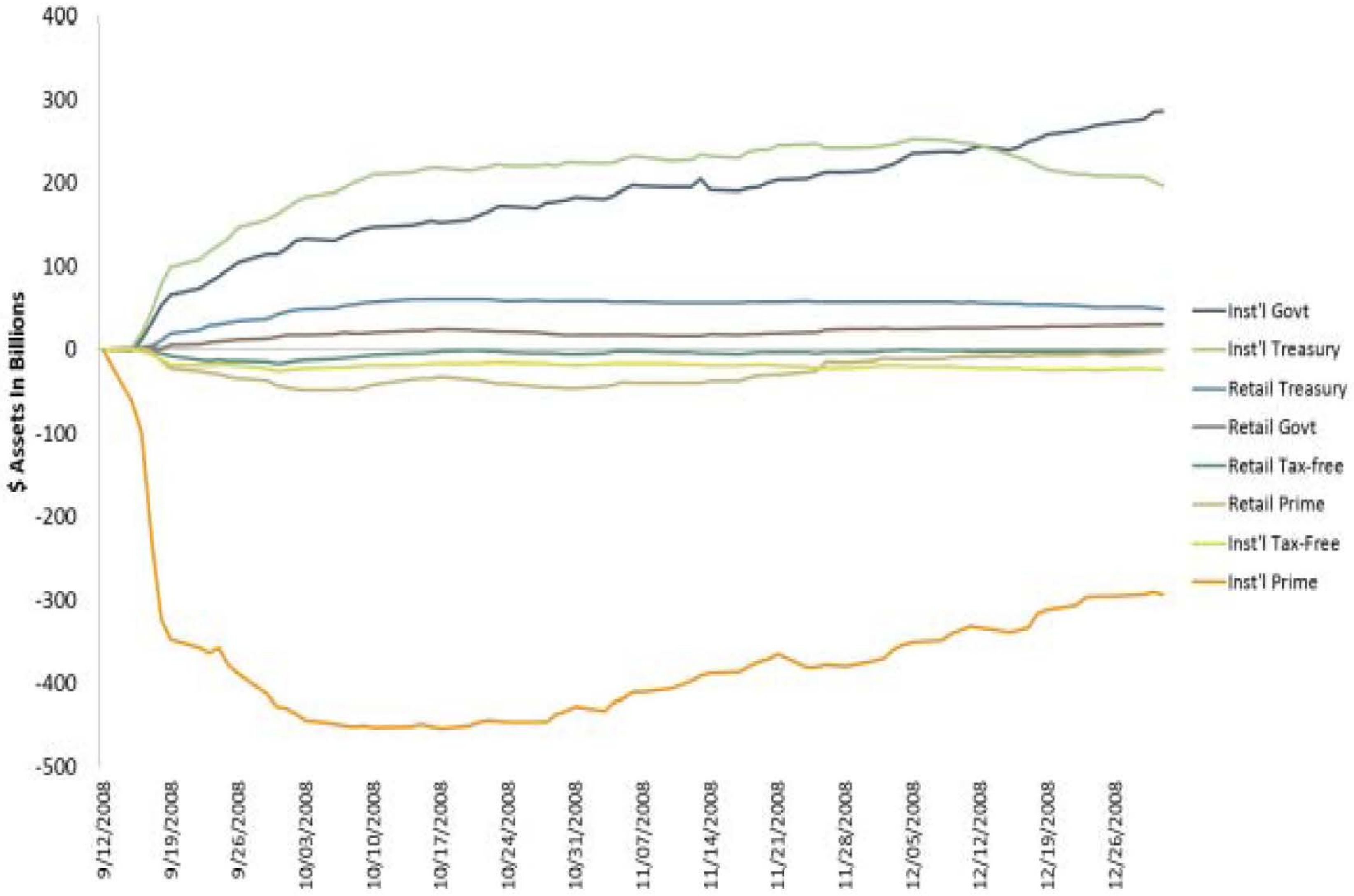
Comparison of Money Market Funds and Banks

		Money Market Funds	Banks
Business Model		Pool cash to enable a broad base of investors access to a market-based short-term interest rate.	Borrow short and lend long to earn an interest rate spread.
Approach		Invest shareholder liquid assets in high quality short-term securities.	Take deposits and short- and long-term wholesale funding to make long-term loans and manage a portfolio of long-term securities.
Assets	**Type**	Repurchase agreements, certificates of deposit, commercial paper, treasury bills, and other high quality short-term debt.	Primary assets include loans (62%) and securities (27%).
	Maturity	Average maturity less than or equal to 60 days (as required by SEC Rule 2a-7).	Loans have an average tenor in the 2 to 5 year range. Securities are predominantly 3 years and longer. 30% of securities are longer than 15 years.
	Quality	Credit quality of typical portfolio is AA-.	Loan delinquency and loss rates are most comparable to public issuers rated in the B to BB categories. Securities are of varying credit quality.
Use of Borrowed Money		No - investors effectively have a pro-rata interest in the investments of the fund.	Yes - banks utilize borrowed money to create leverage typically on the order of 10 times.
Disclosure		Monthly holdings of every security posted on website with more detailed monthly reporting to SEC on Form N-MFP with five days of month end. Daily market value NAVs posted by many firms.	Quarterly, regulatory filings made to FDIC, Federal Reserve and SEC depicting security and loan exposures in high level categories within 40-45 days of quarter end without specific portfolio disclosure to public markets.
Federal Insurance		None	Deposits insured up to $250,000

Source: Fidelity as of July 2011

Money Market Funds Reacted Differently During Crisis



Source: iMoneyNet

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Exclude Treasury / Government / Municipal / Prime Retail MMFs from Further Reform

- **There are vast differences in portfolio composition, liquidity, and risk profiles across the different types of MMFs**
  - SEC study: Confirmed that not all MMFs are the same and that different types of funds perform differently during times of financial stress
  - FSOC Recommendations: Acknowledged that the more sophisticated, risk-adverse institutional investors accounted for 95% of the net redemptions from Prime funds

- **The only type of MMFs that experienced significant outflows in 2008 were Prime funds purchased primarily by institutional investors**
  - Institutional Prime funds lost 26% of assets, or just under $350 billion
  - Treasury and Government funds actually had large inflows – in a “flight to quality” – of over $185 billion, or almost 30% of total assets
  - Municipal funds had modest outflows of less than 5% (~$26 billion)
  - Retail Prime funds experienced less than 3% of outflows (~$20 billion)

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Triggered Liquidity Gates and/or Fees More Effective

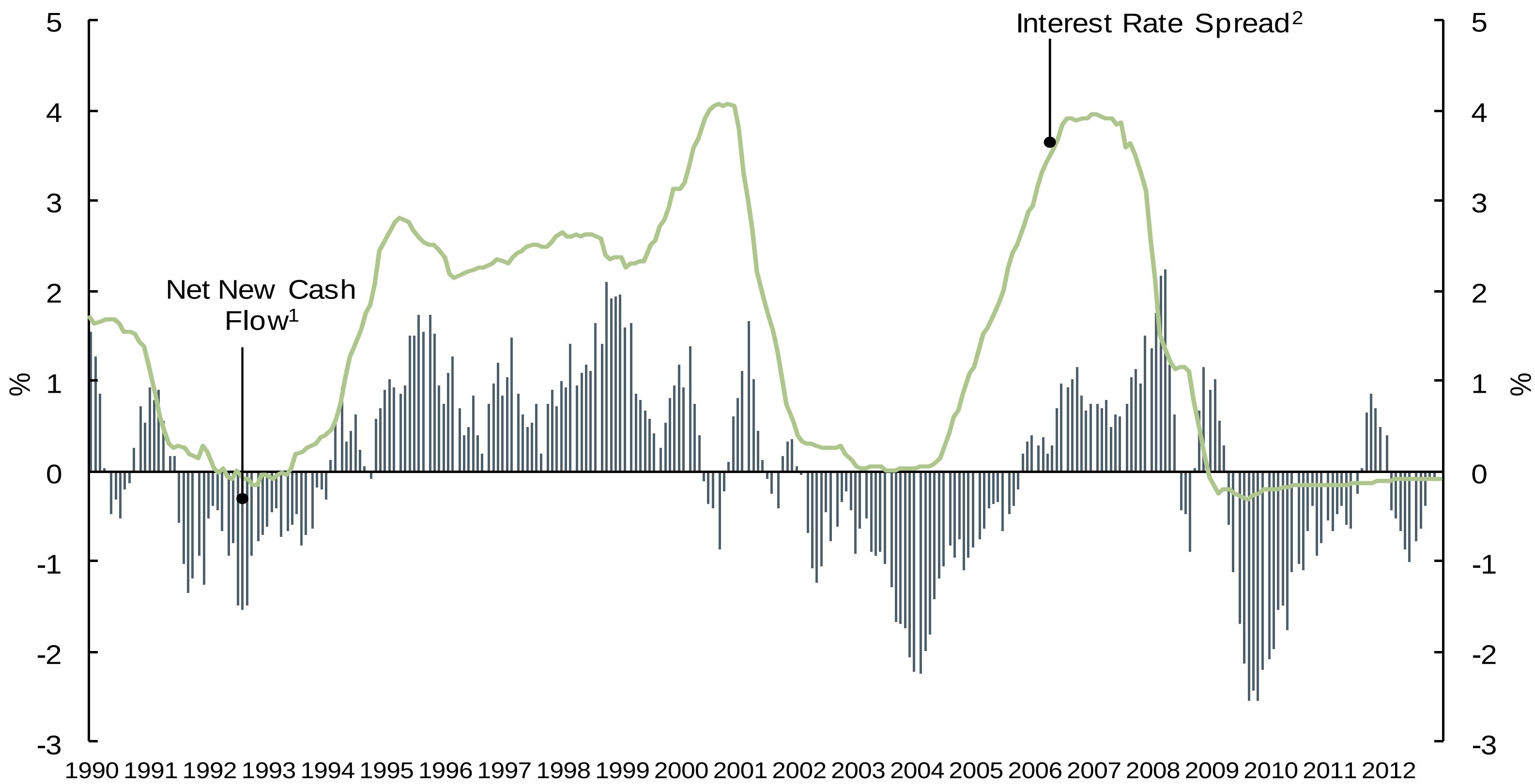
- **If the SEC concludes that Institutional Prime MMFs need further reform, a better approach would be requiring liquidity gates and/or fees that would be triggered only during times of market stress**
  - If weekly liquid assets fell below a certain threshold, fund would temporarily suspend redemptions to allow the fund to restore its health
  - If weekly liquidity level continued to fall below another predetermined threshold, shareholders would have the option to redeem, subject to a fixed redemption fee of 1%
  - Imposing a redemption fee would compensate the fund and its remaining shareholders for the costs of withdrawing liquidity from the fund

- **During times of market stress, halting redemptions or charging a fee when liquidity is scarce is the only effective means of stopping large, sudden outflows**

Appendix

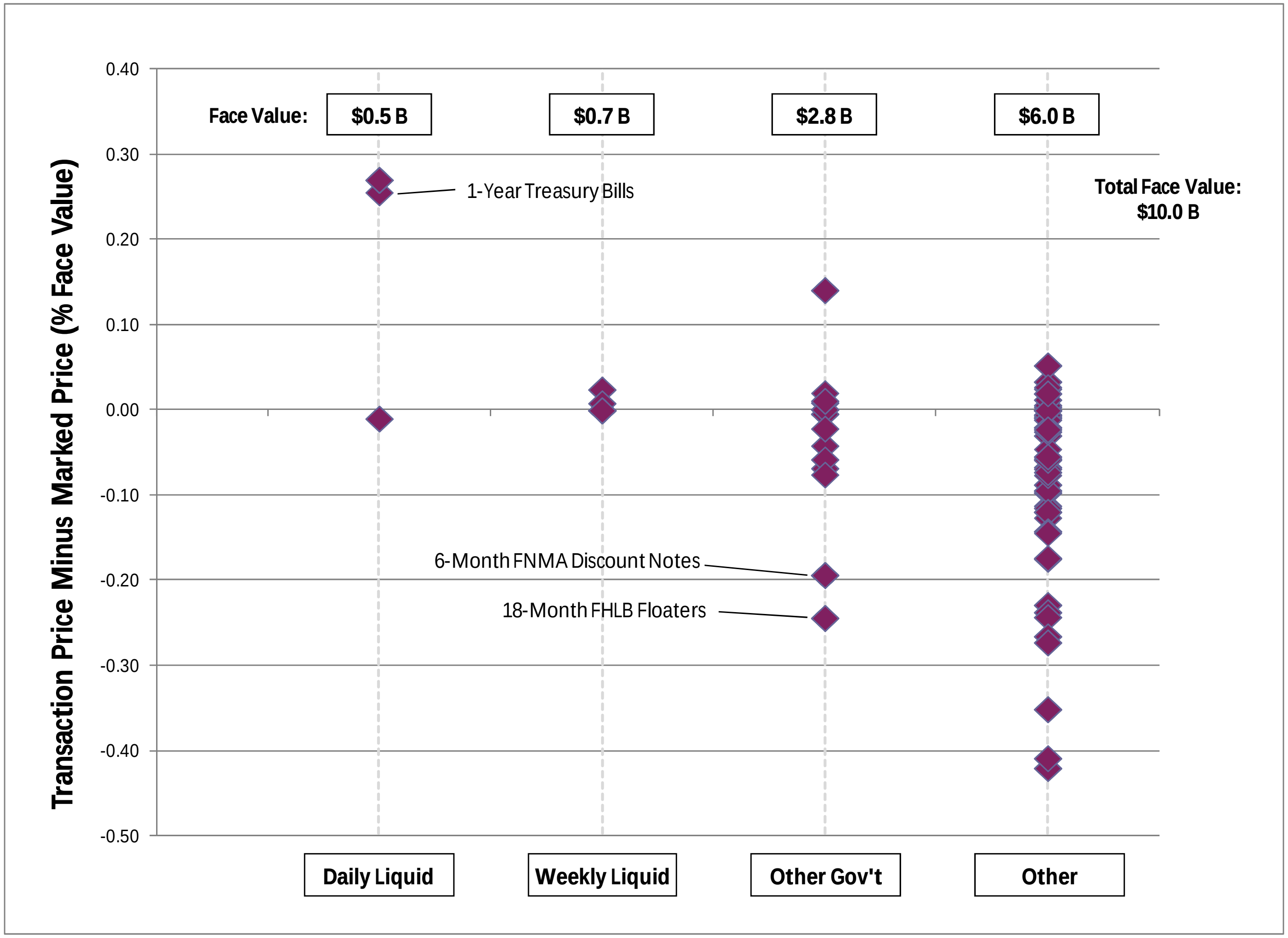
Yield Differentials Drive Flows

PRIME MONEY MARKET FUND YIELDS AND FLOWS RELATIVE TO BANKS



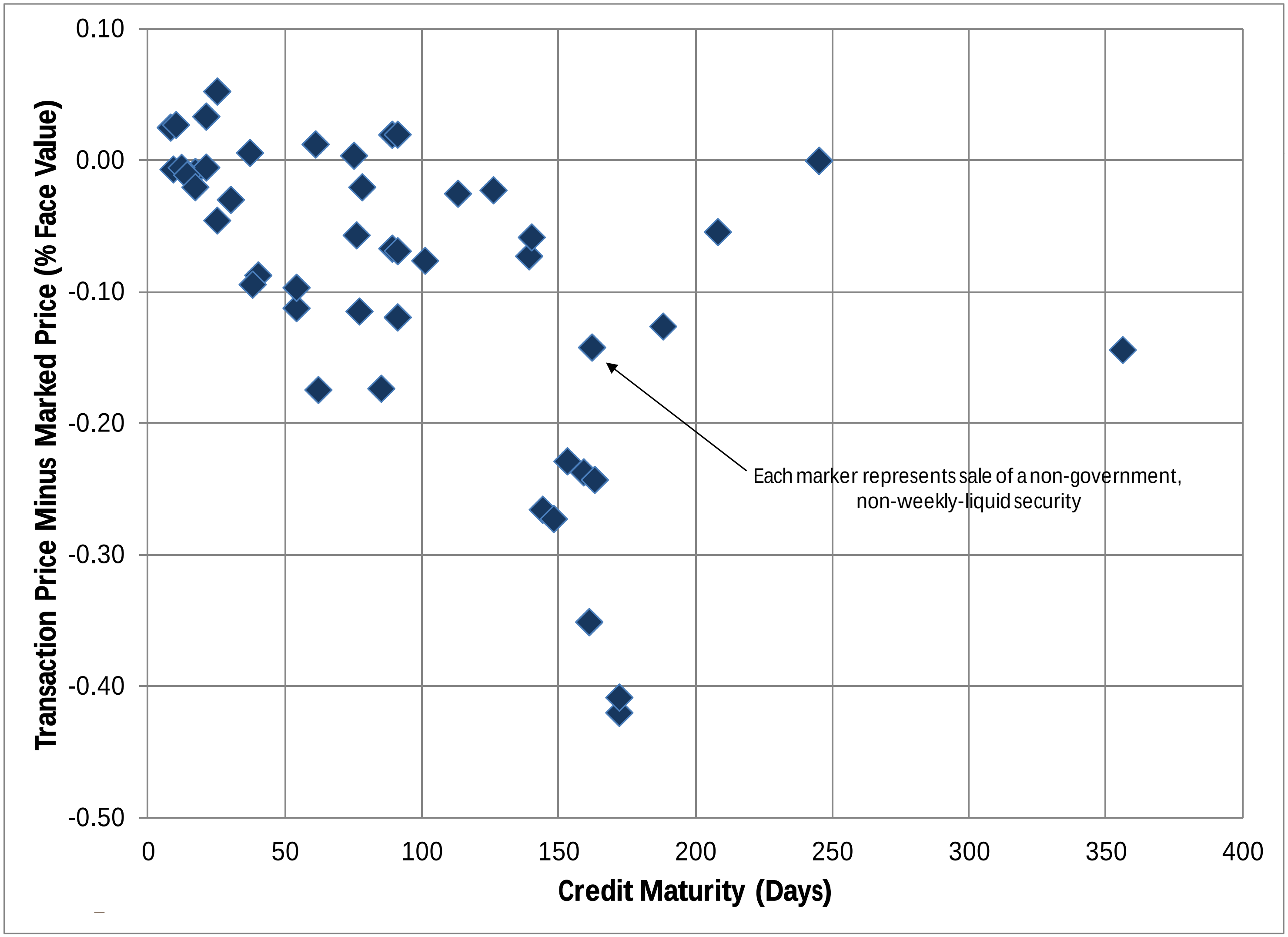
[1] Net new cash flow is a percent of previous month-end taxable retail money market fund assets and is shown as a six-month moving average
[2] The interest rate spread is the difference between the taxable retail money market fund yield and the average interest rate on money market deposit accounts
Sources: Investment Company Institute, iMoneyNet, and Bank Rate Monitor as of 12/31/12

Security Sales During Week Following Lehman Bankruptcy (Sep 15, 2008 – Sep 19, 2008) By Security Type



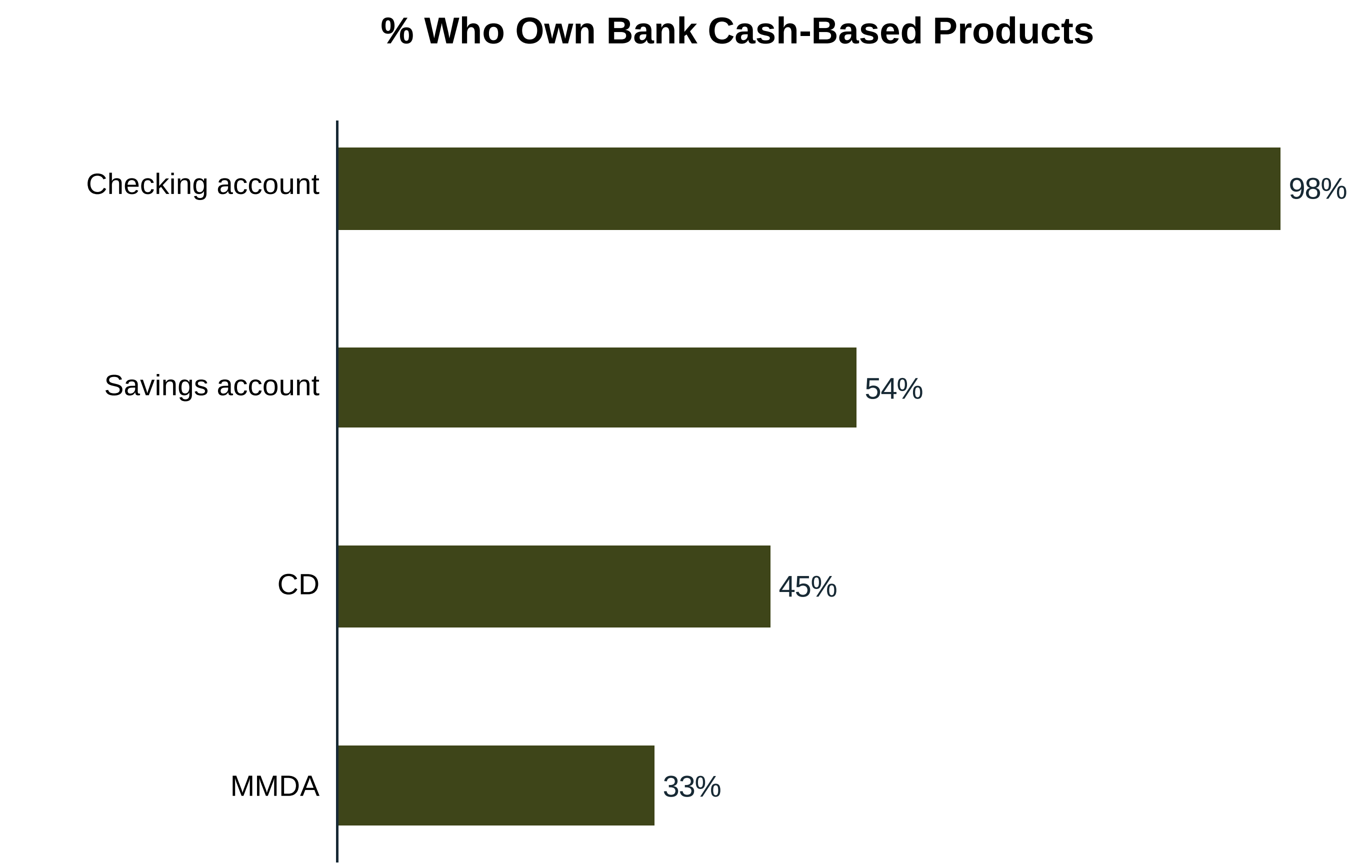
Average price spread (bp):	19	1	-7	-9

Security Sales During Week Following Lehman Bankruptcy By Credit Maturity



Selected Customer Survey Data

Retail Money Market Fund Shareholders Also Own Bank Cash-Based Products



Base: Customers who invest in MMFs outside of tax-deferred account (from any provider)
Source: Fidelity Customer Survey – July 2011

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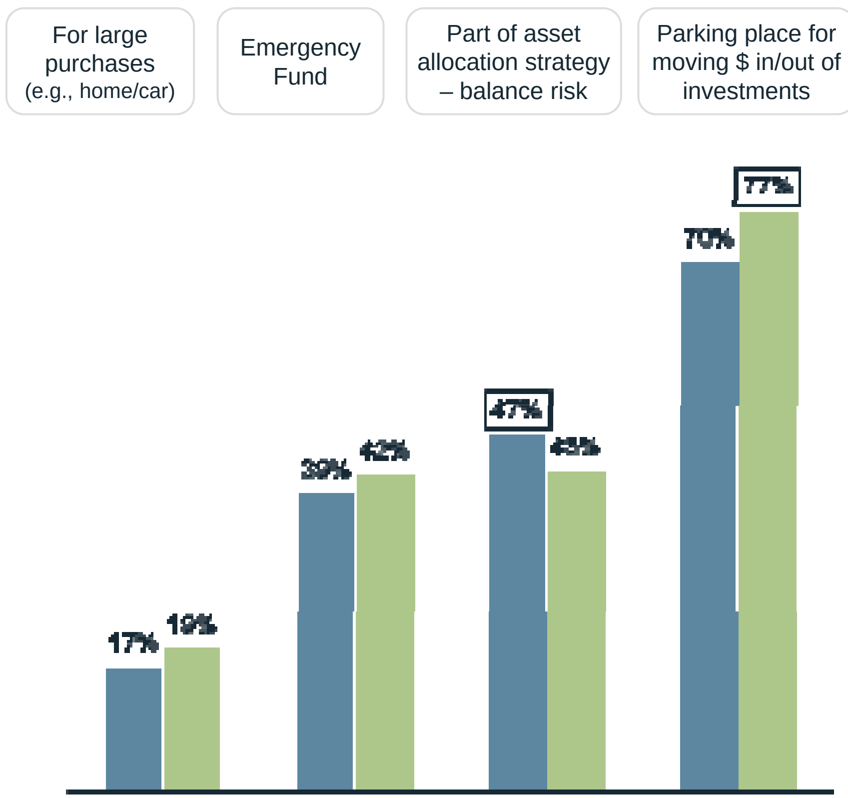
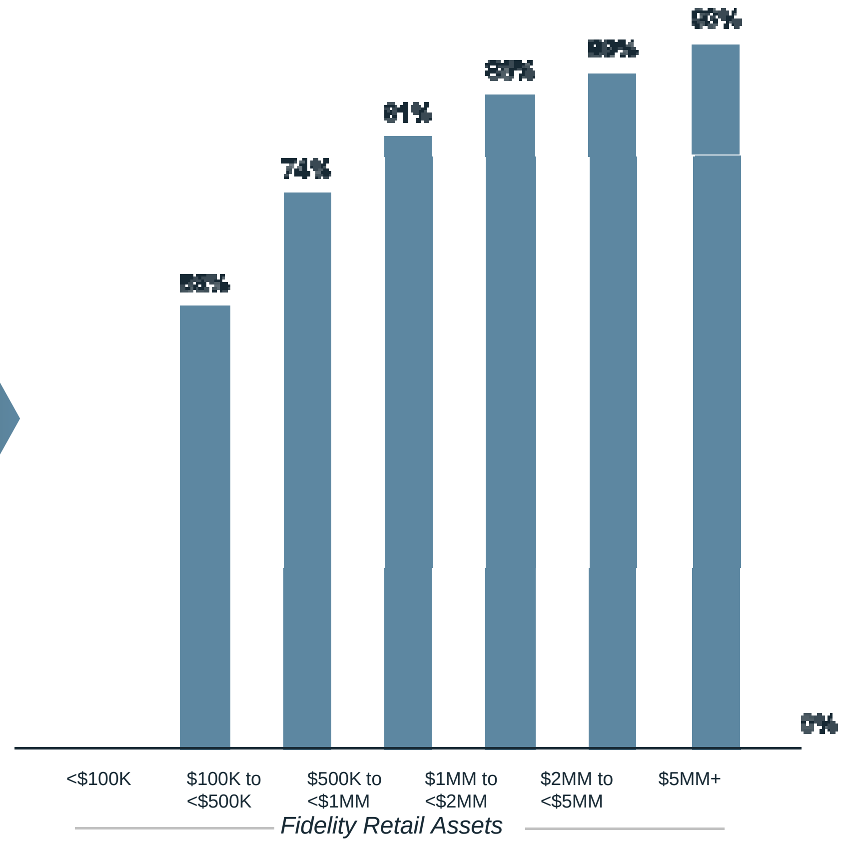
MMFs Are Primarily Used as a "Parking Place" for Investments

Key Reasons Customers Use MMFs

Uses of Money Market Mutual Funds



Use as "Parking Place" by Fidelity Asset Level



Total Retail Affluent

☐ = significantly higher than other group

Base: Fidelity customers w/MMF (from any provider); Affluent=Fidelity assets $100K+

Source: Feb 2012 customer survey, Q11

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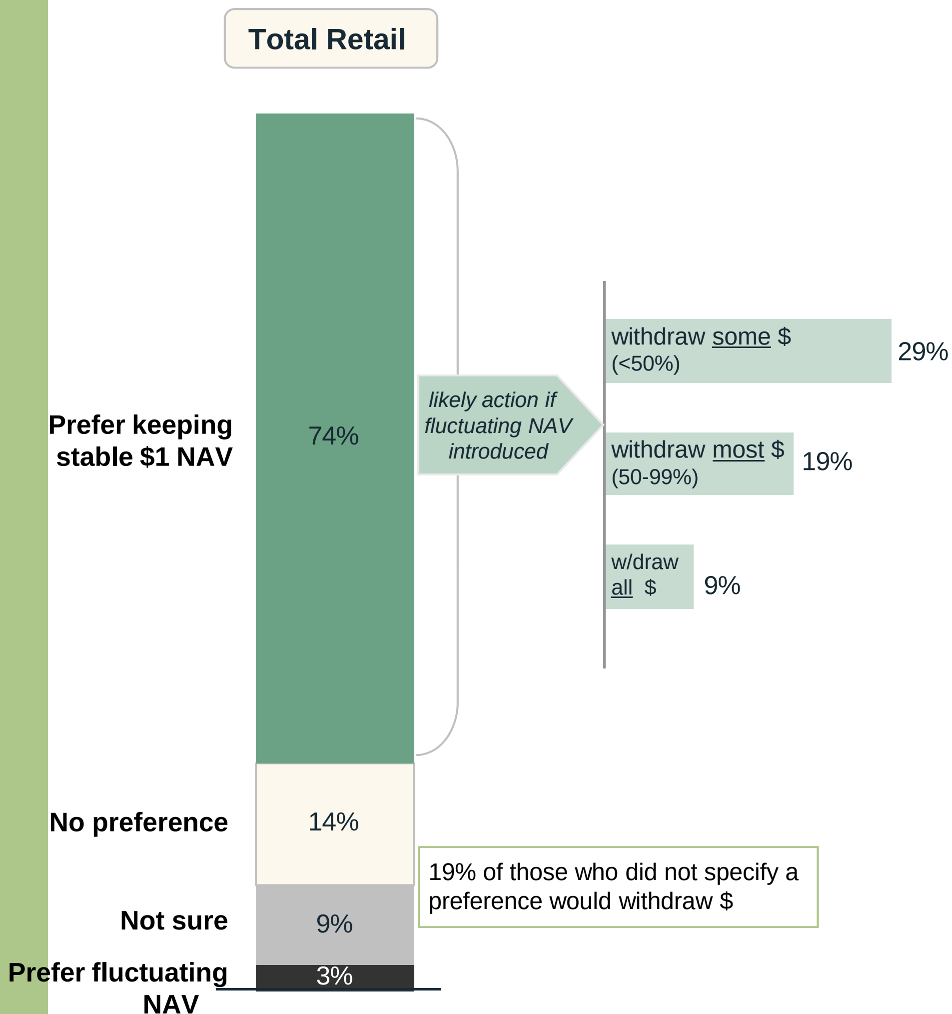
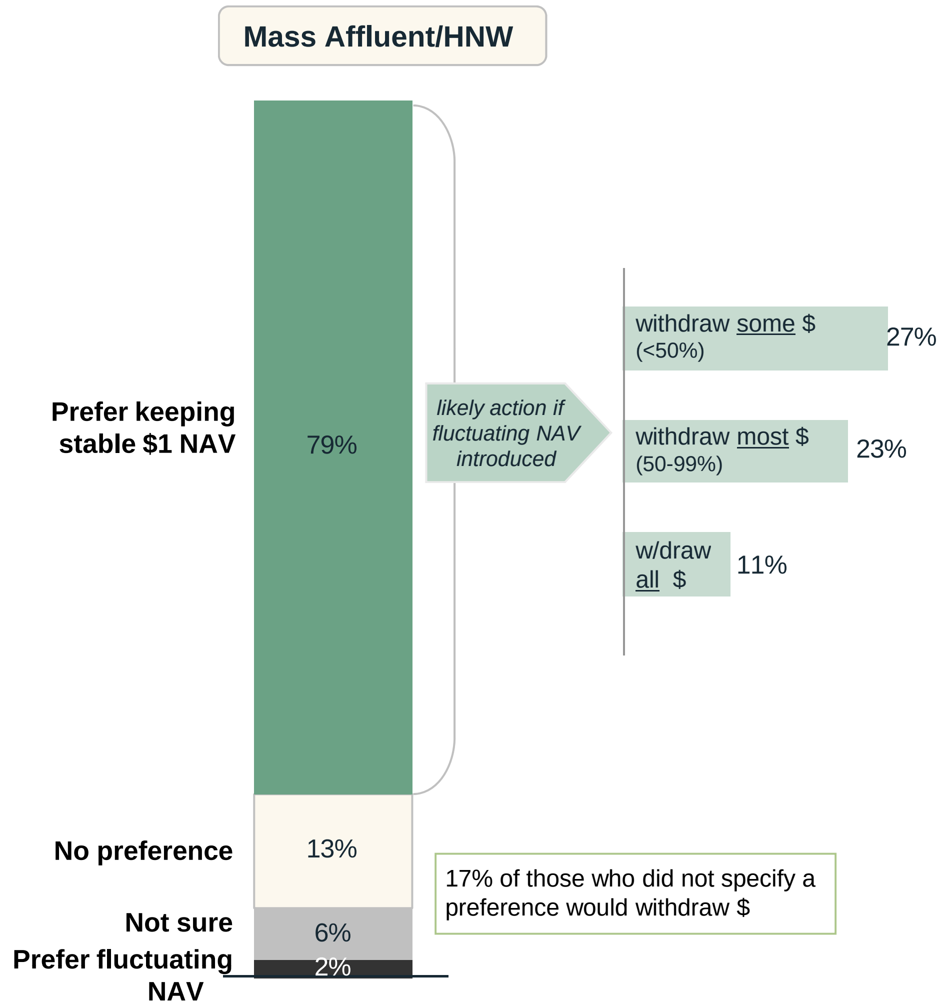
Retail Money Market Fund Investors Will Withdraw Cash if NAV Floats





Base: Currently invest in MMFs outside of tax-deferred account (from any provider)
Total=Fidelity assets $2K+, Mass Affluent/HNW =Fidelity assets $100K+

Source: Fidelity Customer Survey – April 2011

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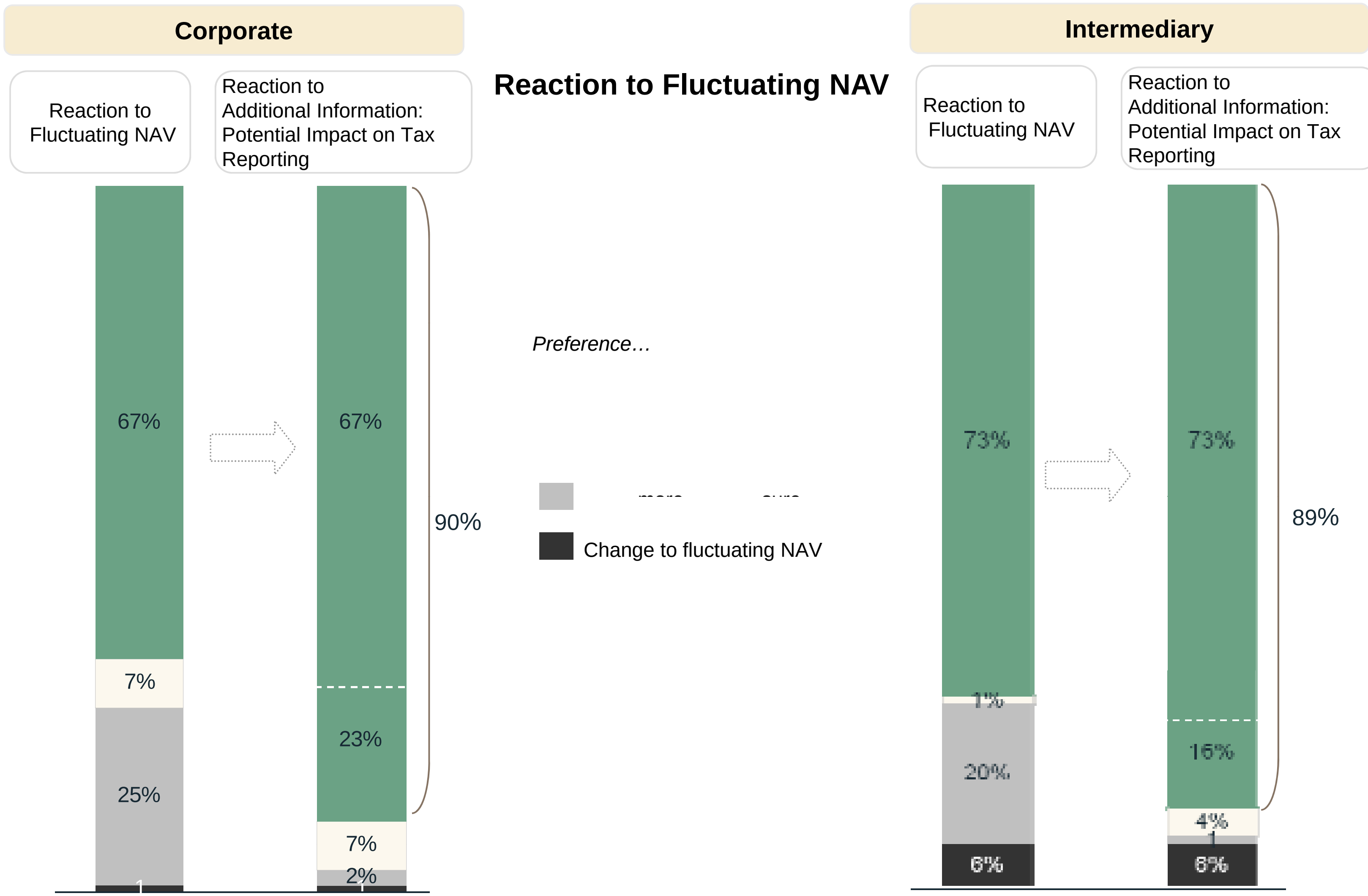
Institutional Clients Have Strong Preference for Stable $1 NAV -- Especially as They Become More Informed



Note: Those not familiar with Fluctuating NAV were provided a description
Corporate = primarily Treasurers, purchase MMFs directly;
Intermediary = within bank, have selling agreement w/Fidelity and can recommend to Institutional clients
Source: FFAS Institutional Client survey – Jul/Aug 2011;

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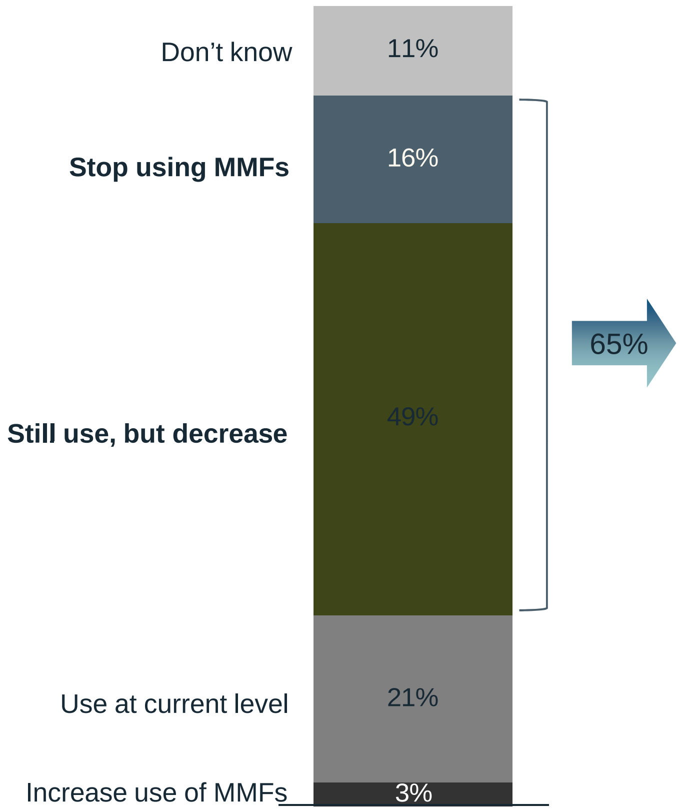
Floating NAV Would Impact MMF Use by Intermediaries -- Leading to Potential Concentration Risk at Banks

Impact of Fluctuating NAV on Use of MMFs – Intermediary MMF Clients



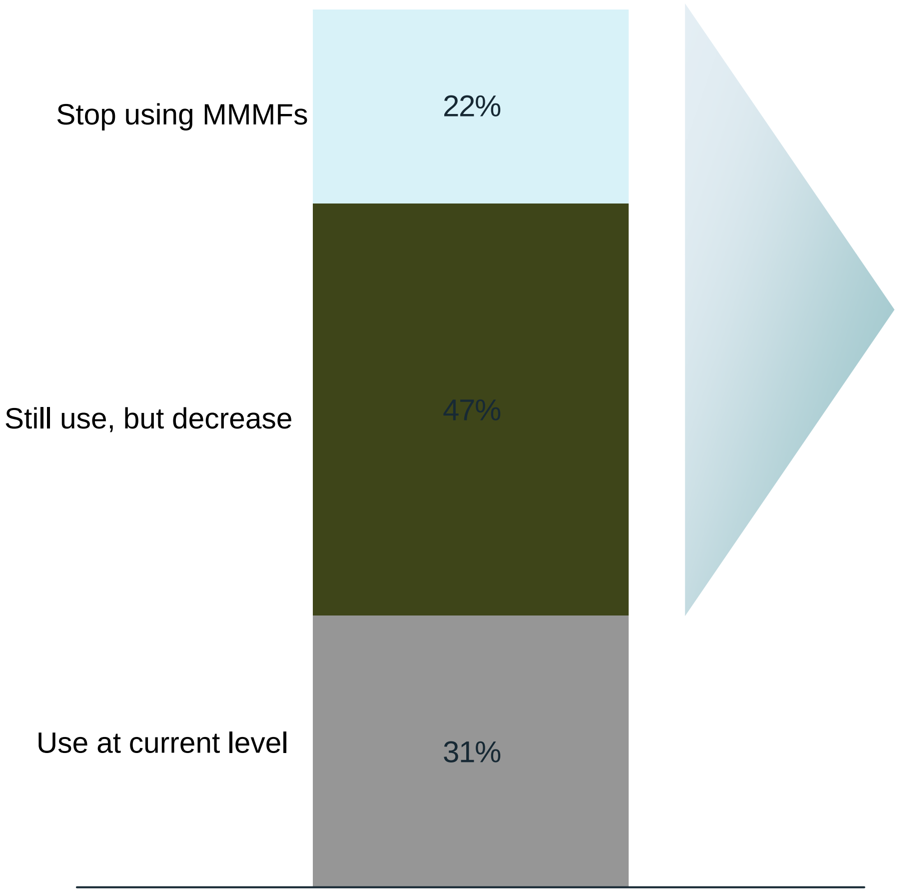
Investments They Would Use Instead of MMFs*
(among those who would decrease/stop using)

	Would Use	Primary Type
• Treasury Securities	89%	16%
• Bank MMDA	84%	49%
• CDs	80%	--
• Commercial Paper	78%	16%
• Time Deposits	76%	9%
• Non 2a-7 funds with 1-yr or shorter WAM	27%	--
• Offshore Funds	20%	--
• Separately Managed Accts	20%	--
• Cash	4%	

Intermediary = within bank, have selling agreement w/Fidelity and can recommend to Institutional clients
*Would use = multiple types allowed; primary = select one type, 10% did not indicate primary type;
Source: FFAS Institutional Client survey – Jul/Aug 2011

A Floating NAV Would Drive Institutional Investors to Money Market Instruments and FDIC Products

Likely Actions
If Fluctuating Share Price Introduced



Investments They Would Use
Instead of MMMFs

- Short-term instruments 74%
  (e.g., CP, ABCP, Repo, Time Deposits)
- Bank MMDA 58%
- CD 54%
- Other 12%
  (primarily indicated Treasuries)

Source: Money Market Fund Institutional Investor Survey – August 2009

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