MEMORANDUM

To: Money Market Fund Reform Proposal File

From: Brian McLaughlin Johnson
Senior Counsel, Division of Investment Management

Date: September 16, 2013

Re: Meeting with Representatives of the Structured Finance Industry Group

On September 10, 2013, Diane Blizzard, Associate Director, Division of Investment Management (IM), Sarah ten Siethoff, Senior Special Counsel (IM), Thoreau Bartmann, Branch Chief (IM), Brian McLaughlin Johnson, Senior Counsel (IM), David Beaning, Special Counsel, Division of Corporation Finance (CF), Lulu Cheng, Special Counsel (CF), and Christof Stahel, Financial Economist, Division of Economic and Risk Analysis, met with the following representatives of the Structured Finance Industry Group (SFIG): Richard Johns (SFIG Executive Director), Tim Mohan (Chapman and Cutler), Rachel George (Chapman and Cutler), Doug McCormack (Sidley Austin), Sam Pilcer (Credit Agricole), Randy Harrison (Citigroup), Eric Wise (RBC Capital Markets), and Jeff BaCote (BMO Capital Markets). The representatives discussed the Commission's proposal on money market fund reform.

Impact of Proposed Revisions to Rule 2a-7 on Asset-Backed Securities

U.S. Securities and Exchange Commission

September 10, 2013

Structured Finance Industry Group

SEC Proposed Revisions to Rule 2a-7

On June 5, 2013, the SEC proposed revisions to Rule 2a-7 under the Investment Company Act of 1940 (the **"Rule"**). If adopted as proposed, these changes would affect asset-backed securities (**ABS**) in five significant ways:

1. Special purpose entities that are affiliated by equity ownership would be treated as a single issuer for purposes of the Rule's 5% issuer diversification requirement (the "**proposed affiliate rule**").

2. A sponsor of an ABS would be treated as a guarantor of the ABS unless the board of directors of the money market fund (**MMF**) made a determination that the fund did not rely on the sponsor's financial strength for credit or liquidity purposes (the "**proposed sponsor rule**").

3. Sponsors treated as guarantors under these new provisions would no longer be "non-controlled persons" for purposes of the Rule's guarantor diversification requirements.

4. The proposed sponsor rule would presumably apply in determining what entities are guarantors of 10% obligors for purposes of the Rule.

5. The new affiliate rule would presumably apply in determining what entities are 10% obligors of ABS (and, therefore, issuers for purposes of the 5% issuer diversification requirement).

Impact on Asset-Backed Commercial Paper

The proposed Rule revisions would have a significant impact on asset-backed commercial paper (**ABCP**). In particular:

1. Special purpose entities that are affiliated by equity ownership would be treated as a single issuer for purposes of the proposed affiliate rule. *ABCP conduits with different administrators and credit and liquidity support providers but common nominal equity owners would be treated single issuers under this provision.*

2. The sponsor of an ABCP conduit would be treated as a guarantor of all of the conduit's ABCP unless the board of directors of the MMF made a determination that the fund did not rely on the sponsor's financial strength for credit or liquidity purposes. *The guaranteed portion of ABCP issued by partially-supported ABCP conduits under the Rule would increase dramatically as compared to the current Rule.*

3. Sponsors of ABCP conduits treated as guarantors under these new provisions would no longer be "non-controlled persons" for purposes of the Rule's guarantor diversification requirements. *This would require both fully- and partially-supported ABCP conduits to comply with both the issuer diversification rule and the guarantor diversification rule.*

4. The proposed sponsor rule presumably would apply in determining what entities are guarantors of 10% obligors for purposes of the Rule. *Because the ABCP conduit sponsor would be treated as a controlled person as described above, this analysis would need to be made regardless of the credit and liquidity support provided by the sponsor.*

5. The new affiliate rule would presumably apply in determining what entities are 10% obligors of ABS (and, therefore, issuers for purposes of the 5% issuer diversification requirement). *Because the ABCP conduit sponsor would be treated as a controlled person as described above, this analysis would need to be made regardless of the credit and liquidity support provided by the sponsor.*

Money Market Funds Hold Significant Amounts of ABCP

- As of July 31, 2013, MMFs held over $94 billion[1] of ABCP representing over 36% of the overall $260 billion ABCP market. [2]

1 Source: Crane Data: *Money Fund Intelligence* (as of July 31, 2013).

2 Source: The Board of Governors of the Federal Reserve System (reporting not seasonally adjusted ABCP outstanding of $259.8 billion as of July 31, 2013) (*available at* http://www.federalreserve.gov/releases/cp/).

ABCP Conduits Provide Significant Financing to the Real Economy

- ABCP is a vital source of low-cost working capital for businesses of all kinds both in the United States and globally, from industrial companies to finance and service companies to governmental entities. Assets funded through these vehicles include trade receivables, auto loans and leases, equipment loans and leases, student loans, credit card receivables, consumer loans and many other types of financial assets.
- For example, as of March 31, 2013, multi-seller asset-backed commercial paper conduits financed approximately $53 billion of trade receivables, $59 billion in auto loan and lease receivables, $6.5 billion of equipment loans and leases, $11 billion of student loans and $15 billion of credit card and consumer loan receivables.
- Virtually all of this financing is provided by regulated ABCP conduit sponsor banks, via committed facilities, to their corporate banking clients. These facilities are often the clients' cheapest form of committed financing due to the secured nature of the transaction and the credit enhancements required by sponsor banks.

Overview of ABCP Conduit Programs

- ABCP programs are financing vehicles that fund a pool of assets with the benefit of liquidity and credit enhancement support (as needed) allowing for the issuance of asset backed commercial paper.

- A financial institution, finance company or other entity establishes a special-purpose, bankruptcy-remote vehicle (an “**ABCP conduit**”) to purchase receivables or receivables interests (which may take the form of an asset-backed security) issued by customers of the financial institution or finance company. The ABCP conduit issues short-term debt (**ABCP**) and uses proceeds to invest in a diverse pool of ABS or to otherwise provide funding to customers of the entity that established the conduit.

- Each transaction funded will typically benefit from a layer of credit enhancement (sometimes in the full amount of the funded transaction) provided by the originator of the assets (or one or more affiliates thereof) or, in the case of fully-supported conduits, one or more highly rated banks.

Overview of ABCP Conduit Programs *(Continued)*

- Liquidity support will be provided to bridge the gap between the asset cashflows and the short tenor liabilities via committed bank provided liquidity facility.
- This liquidity is provided by highly rated banks (and for fully-supported conduits this liquidity support also provides 100% credit support).
- For partially-supported ABCP conduits, a partial amount of program-wide credit enhancement is provided to bridge the gap between amounts funded via the liquidity facility and the outstanding amount of ABCP.

Types of Liquidity Support

- Fully-supported programs are backed by committed 100% liquidity facilities that cover 100% of the ABCP outstanding regardless of the quality of underlying assets.
- Partially-supported programs are backed by committed liquidity facilities that fund advances or asset purchases equal to a defined percentage of non-defaulted receivables. Because the required funding amount under the liquidity facility may be less than the associated ABCP outstanding, program credit enhancement (typically equal to 5-10% of outstanding ABCP) is also provided to the ABCP conduit.

SFIG Concerns with the Proposed Revisions to the Rule 2a-7 Diversification Requirements

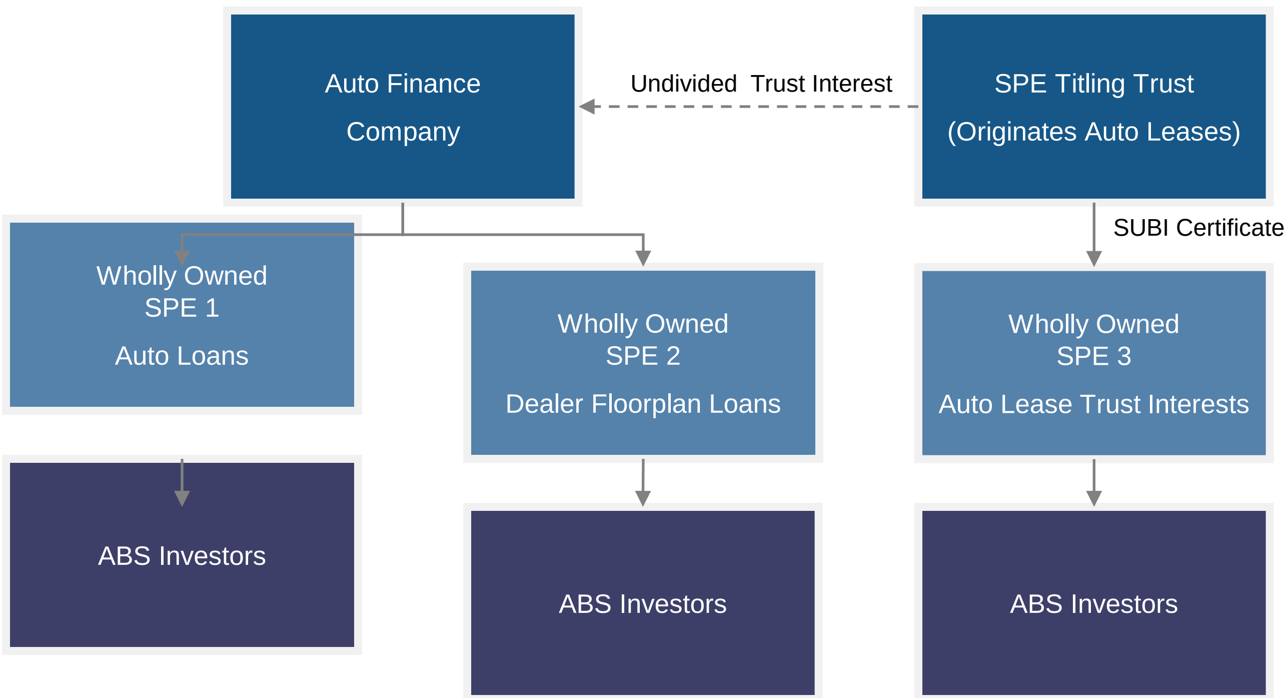
- Application of the proposed affiliate rule to issuers of ABS would have a significant negative impact on both MMFs and ABS issuers.
- The proposed sponsor rule would have a significant impact on the ability of MMFs to invest in ABS and, in particular, ABCP.
- The proposed affiliate rule and the proposed sponsor rule could also have a significant negative impact on the ability of ABCP conduits to provide financing to certain types of entities, such as auto finance companies and other large providers of consumer loans.
- Under the proposed sponsor rule, it may be unclear which entity is the “sponsor” of certain ABCP conduits.
- The change to the definition of “guarantee issued by a non-controlled person” may have unintended consequences.

The Proposed Affiliate Rule

- Under the current Rule, there is no grouping of issuers by affiliation. Each legal entity issuing securities is a separate issuer for purposes of the issuer diversification requirement.
- Under the proposed revisions to the Rule, special purpose entities issuing ABS that are affiliated by 50% or more common ownership would be treated as a single issuer.
- As a result, multiple special purpose entities established by a single originator-seller to fund discrete asset pools would be treated as a single issuer.
- Also as a result, all ABCP conduits owned by an entity in the business of owning special purpose entities and their respective affiliates, for example, would be treated as a single issuer even though such ABCP conduits have unaffiliated administrators and credit and liquidity support providers. These equity holders do not and cannot provide any meaningful financial support to the conduits they own.

The Proposed Affiliate Rule:
ABS Originator-Sellers Do Not Guarantee ABS

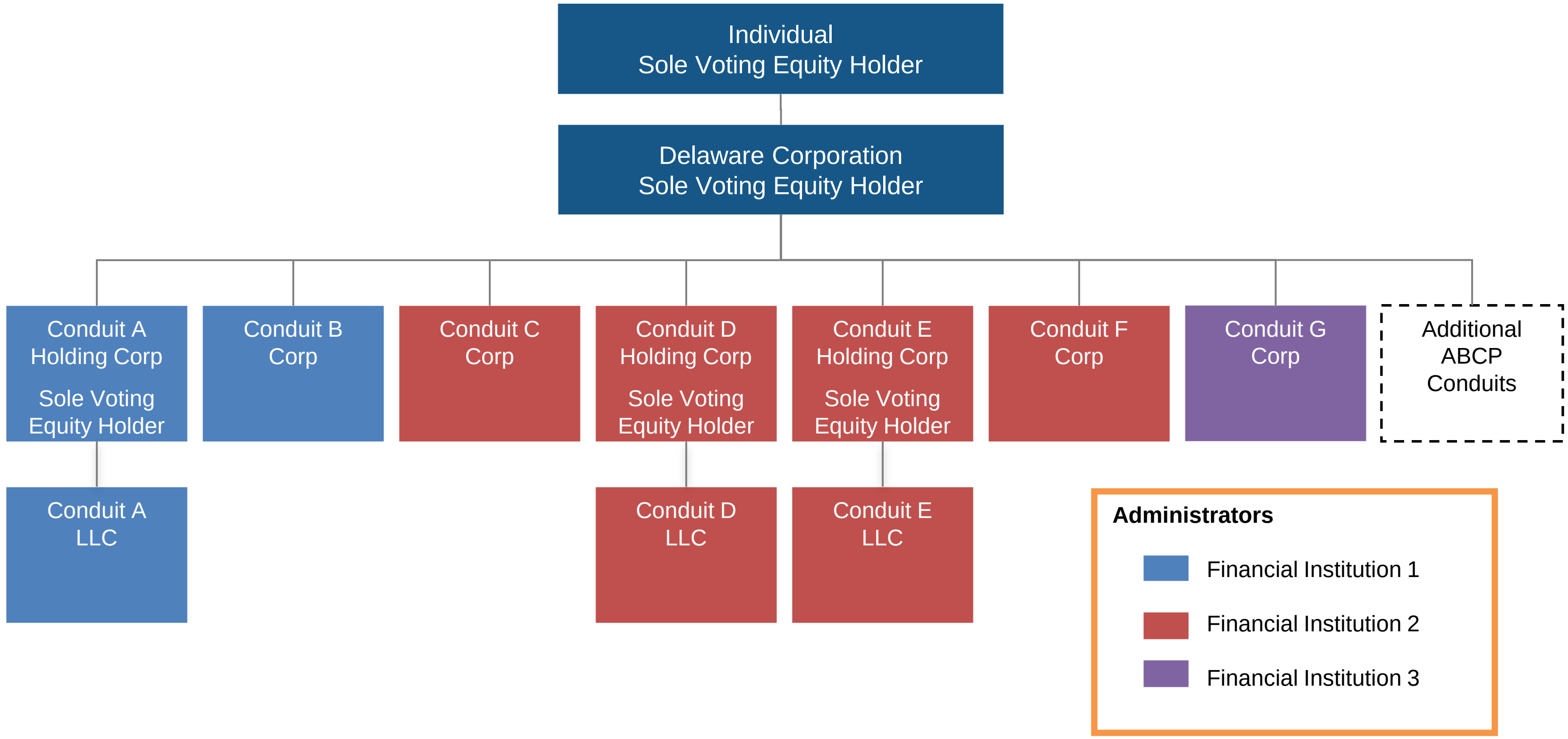
- In the context of ABS other than ABCP, originator-sellers often establish multiple SPEs to fund discrete asset pools. These originator-sellers do not guarantee the issued ABS or the creditworthiness of the securitized assets. Therefore it does not seem appropriate to treat these SPEs as a single issuer.



The Proposed Affiliate Rule: Equity Interests in ABCP Conduits of Multiple Separate Financial Institutions Owned by a Single Entity

Impact on ABCP

- A small number of entities in the business of owning SPEs own the equity interests in multiple ABCP conduits sponsored by separate financial institutions. For example, one company informed us that it owns the equity interest in 35 ABCP conduits sponsored by 21 unaffiliated financial institutions. Another company informed us it owns the equity interests in 17 ABCP conduits sponsored by 10 unaffiliated financial institutions. Under the proposed rules, MMFs would be required to aggregate exposure to all 35 and 17 of these ABCP conduits, respectively.



The Proposed Sponsor Rule:
Impact on ABCP Conduits

Proposed Revisions to the Rule

▪Under the proposed revisions to the Rule, a MMF would be required to treat the sponsor of an ABCP conduit as a guarantor of the ABCP for purposes of the guarantor diversification requirements.

▪Unless the MMF board determined that it was not relying on the sponsor for liquidity or credit (which is unlikely), the sponsor would be a guarantor of 100% of the ABCP.

▪However, under the proposed revisions to the Rule as drafted, the sponsor would no longer be a non-controlled person. As a result, the ABCP conduit would be the issuer of 100% of its ABCP (assuming no 10% obligor) for purposes of the issuer diversification requirement regardless of any sponsor guarantee.

Comparison to Current Rule

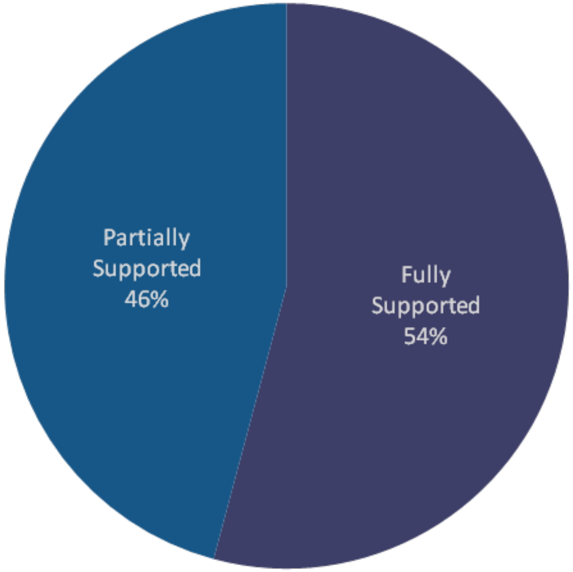
▪Currently, for partially-supported ABCP conduit programs, a MMF would treat only the amount of ABCP covered by the program credit enhancement and any fully-supported liquidity facilities provided by the sponsor as guaranteed. For example, for an ABCP conduit with $10 billion in outstanding ABCP and a $1 billion letter of credit provided by its sponsor as program credit enhancement, a MMF would allocate 10% of its ABCP holdings of such conduit to the sponsor as guarantor.

▪Under the proposed revisions to the Rule, the MMF would be required to allocate 100% of its ABCP holdings of the same conduit to the sponsor as guarantor.

The Proposed Sponsor Rule: Impact on Ability of MMFs to Invest in ABCP

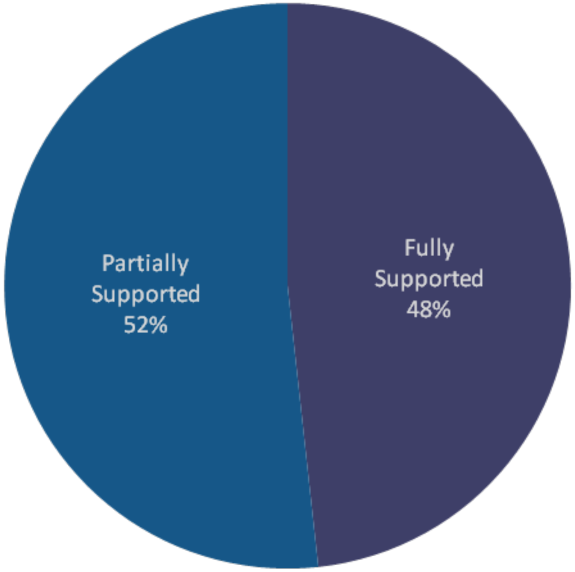
Fully-Supported vs. Partially-Supported ABCP Conduits

By Number of Conduits *(as of 6/30/2013)*



Total = 72 conduits

By Outstandings *(2Q 2013 Average Outstandings)*



Total = $262.3 billion

Source: Moody's 3rd Quarter 2013 ABCP Program Index . Only conduits' U.S. CP issuance was included. Any conduit without U.S. CP issuance was not included. SIVs were not included as any remaining outstandings are not being rolled in the market. Outstandings reflect 2nd Quarter 2013 average.

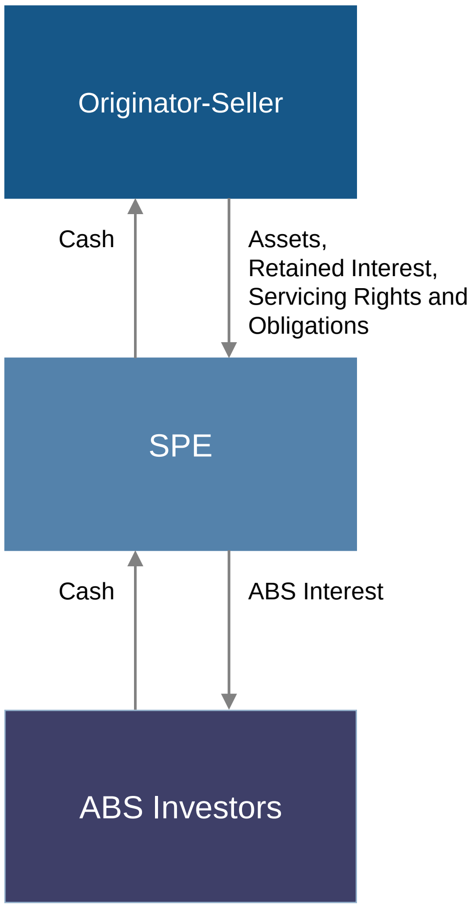
The Proposed Sponsor Rule:
Impact on Ability of MMFs to Invest in ABCP (*Continued*)

- Under the current Rule, the guaranteed portion of a partially-supported ABCP conduit is the amount of its programwide credit enhancement and any additional transaction-specific guarantees.
- As of June 30, 2013, the weighted average required programwide credit enhancement for all partially-supported ABCP conduits was 8% of the outstanding ABCP of such conduits ($128.114 billion as of that date).
- This would mean that on average the amount that an individual MMF could invest in the ABCP of a partially-supported ABCP conduit today theoretically could be as much as 12.5 times more than it could invest under the proposed sponsor rule.

Under the Proposed Sponsor Rule, It May Be Unclear Which Entity is the "Sponsor" of Certain ABCP Conduits

- The SEC's rationale for adopting the proposed sponsor guarantee rule is that financial institutions sponsoring ABCP conduits will provide implicit financial support to these conduits. Where explicit 100% financial support is provided to an ABCP conduit by financial institutions that are not commonly thought of as the "sponsor" (administrator of such conduit), this will not be the case. This issue exists with respect to multi-seller ABCP conduits that are not sponsored by financial institutions and certain single seller ABCP conduits (See Appendix A pp. A-3 and A-4).

The Impact of the Proposed Sponsor Rule on ABS other than ABCP



- Non-ABCP ABS sponsors do not provide credit and liquidity support to related ABS. They are prohibited by bankruptcy structuring principles from providing significant support and are not necessarily incented to provide any implicit support.

Note: No guarantee of securitized assets exists

The Proposed Sponsor Rule:
Should Sponsor be Treated as a “Controlled Person”?

- Where a sponsor “guarantees” the ABCP of an ABCP conduit, by definition the MMF is or should be relying primarily upon the creditworthiness of the sponsor. It would seem to follow from this that the sponsor should therefore be treated as a “non-controlled person” under the Rule and the guaranteed portion of the ABCP should not be subject to the issuer diversification restrictions of the Rule unless the MMF sponsor has made a determination that the fund did not rely on the sponsor’s financial strength for credit or liquidity purposes.

Impact of Proposed Sponsor Rule and Proposed Affiliate Rule on 10% Obligor Rule

Impact of Proposed Affiliate Rule on 10% Obligor Rule

- The proposed affiliate rule would also have an indirect impact on the 10% obligor rule applicable to ABS.
- For ABS, any entity whose obligations constitute 10% or more of the principal amount of the qualifying assets of the primary ABS is deemed to be an issuer of the portion of the primary ABS such obligations represent. Currently, each ABS issued by a separate entity is analyzed separately, and an ABCP conduit typically represents to MMFs that it does not intend to purchase any ABS which would result in a 10% obligor.
- If the proposed affiliate rule is adopted **and** is made applicable to the 10% obligor analysis, it is likely that some of the ABS held by a conduit will need to be aggregated, resulting in 10% obligors.
- Because of the issues associated with 10% obligors, conduits are likely to restructure their activities to avoid having 10% obligors, resulting in decreased funding capacity for important sectors of the economy.

Impact of Proposed Sponsor Rule and Proposed Affiliate Rule on 10% Obligor Rule

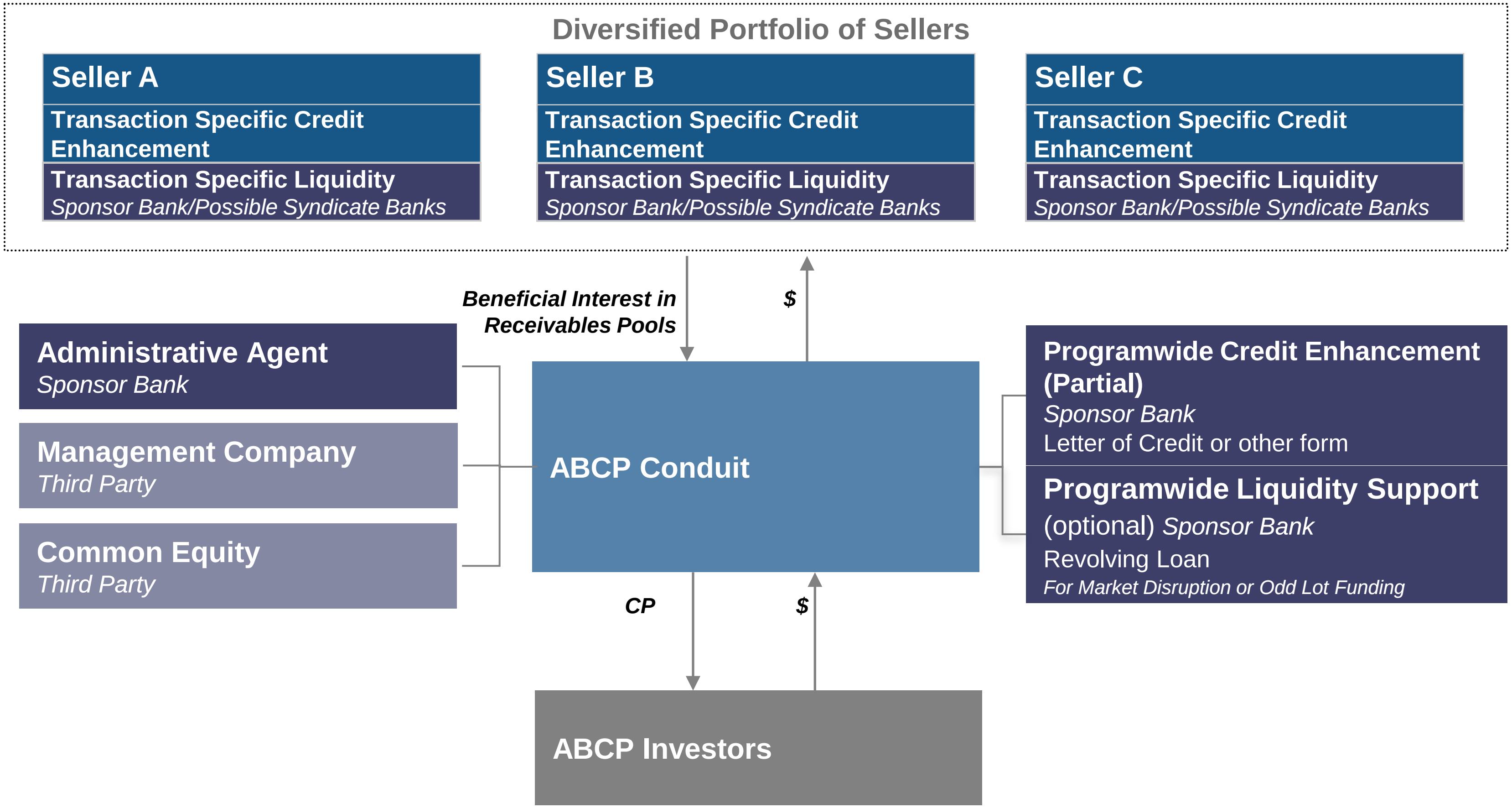
Impact of Proposed Sponsor Rule on 10% Obligor Rule

- The same analysis applies to the proposed sponsor rule: if the proposed sponsor rule is adopted to apply to all ABS and is made applicable to the 10% obligor analysis, it is likely that some of the ABS held by a conduit will need to be aggregated for purposes of reporting guarantors of obligations of 10% obligors. This, again, is a result that will likely be avoided through reduction of financing to current recipients of ABCP conduit funding.

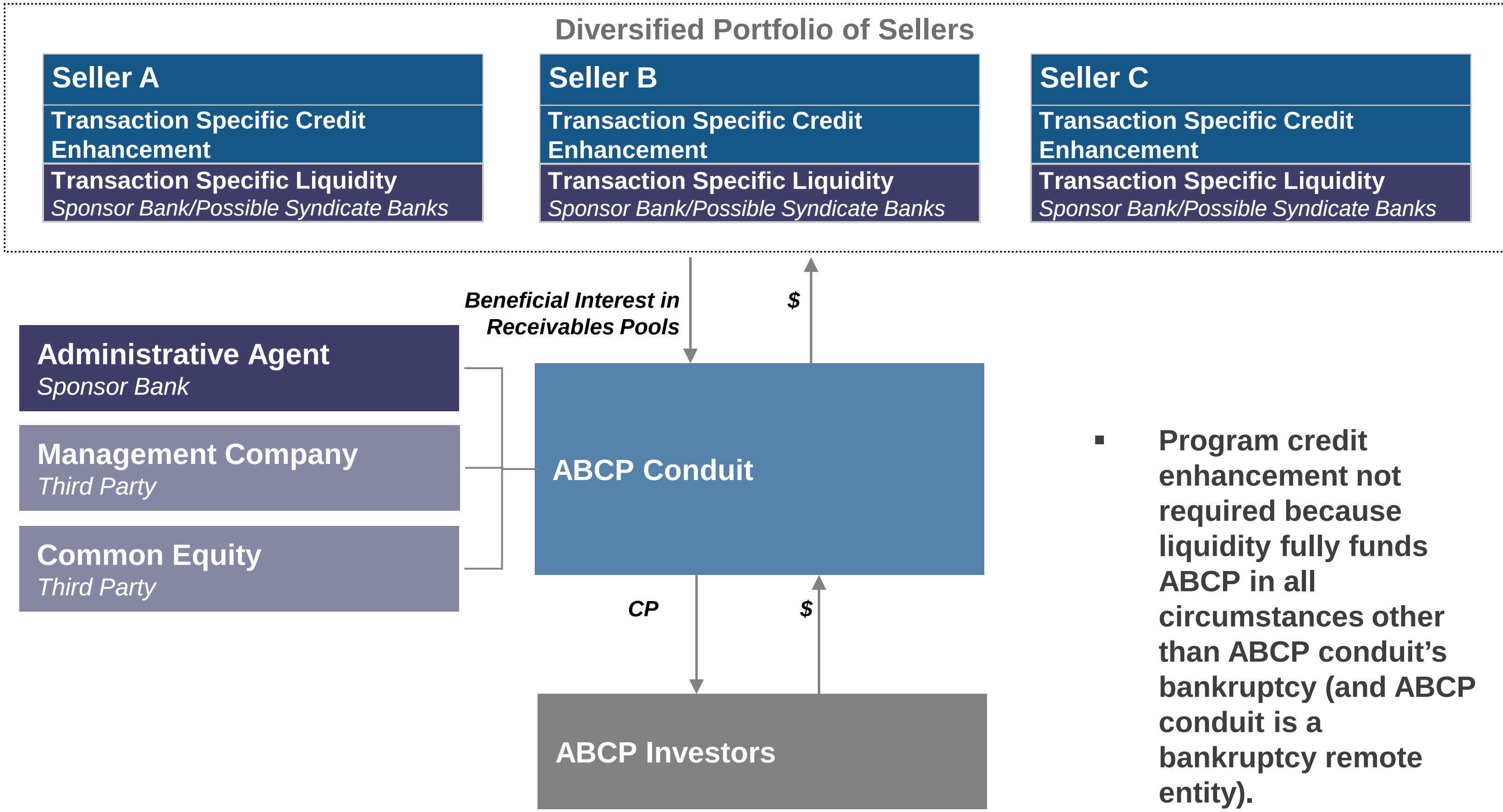
Appendix A:

Typical ABCP Conduit Structures

Example of Bank-Sponsored Partially-Supported Multi-Seller ABCP Conduit Structure

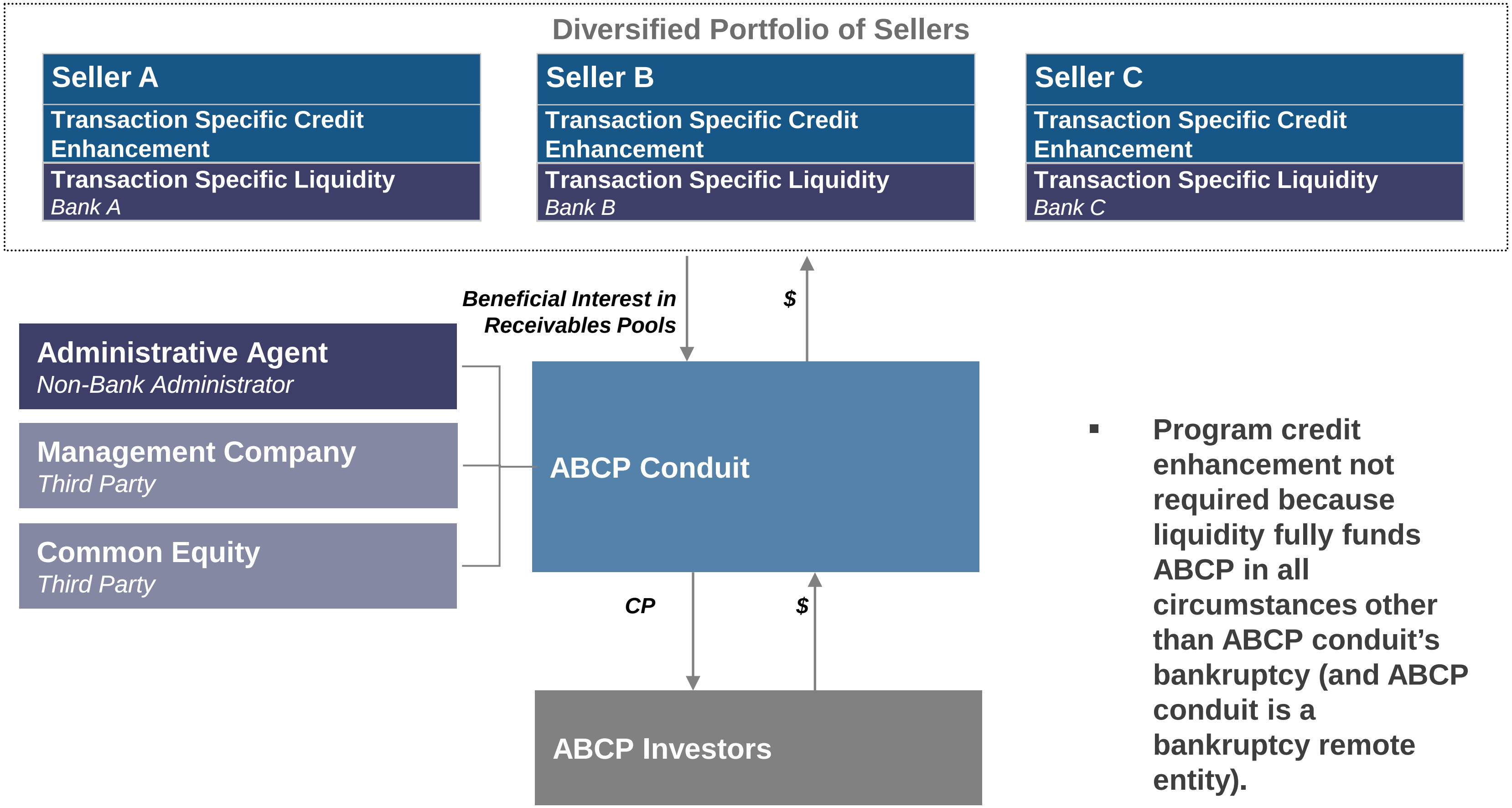


Example of Bank-Sponsored Fully-Supported Multi-Seller ABCP Conduit Structure



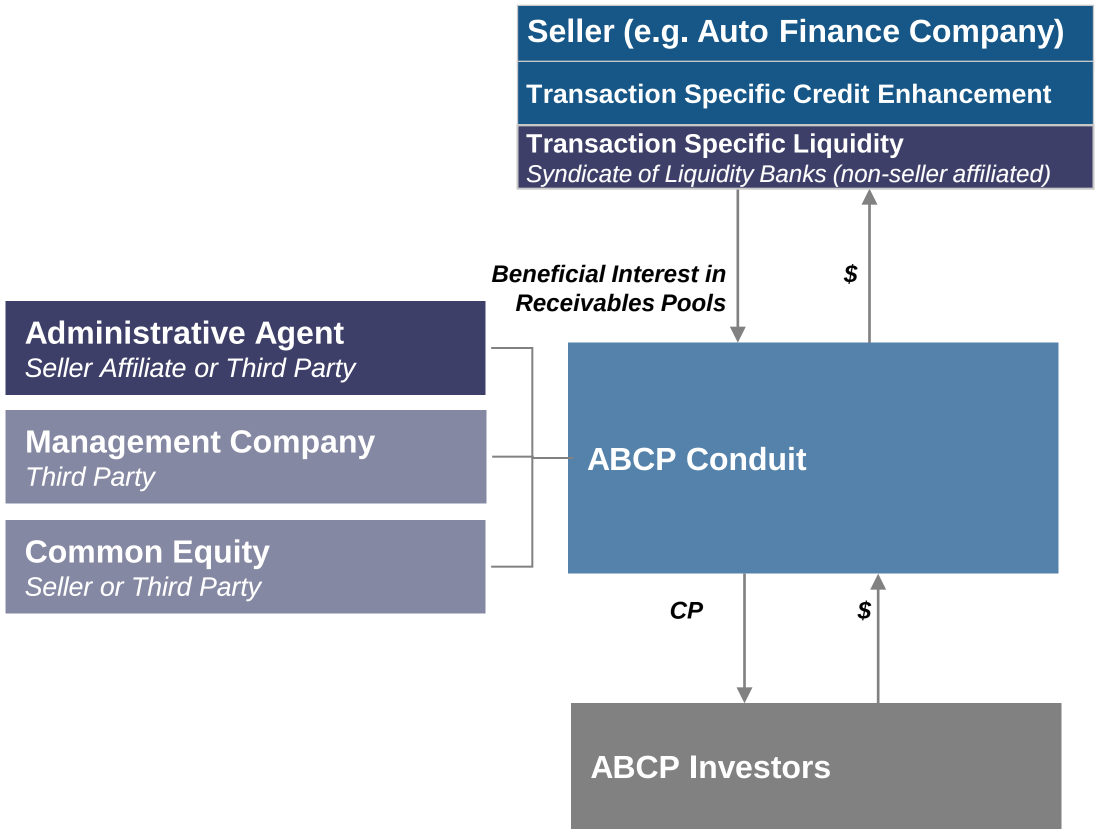
- **Program credit enhancement not required because liquidity fully funds ABCP in all circumstances other than ABCP conduit's bankruptcy (and ABCP conduit is a bankruptcy remote entity).**

Example of Non-Bank Administered Multi-Seller ABCP Conduit Structure



- Program credit enhancement not required because liquidity fully funds ABCP in all circumstances other than ABCP conduit's bankruptcy (and ABCP conduit is a bankruptcy remote entity).

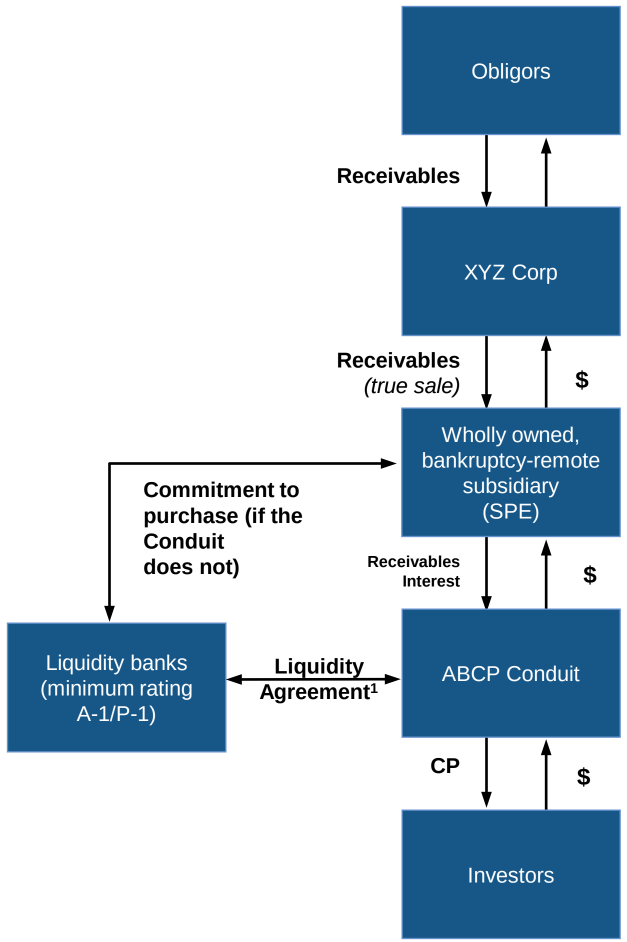
Example of Single Seller ABCP Conduit Structure



Appendix B:

Structural Overview of a Typical ABCP Conduit Transaction

Structural Overview of a Typical ABCP Conduit Transaction



- XYZ Corp establishes a wholly owned, bankruptcy-remote, special purpose entity ("SPE") for the purpose of conducting a securitization
- XYZ Corp and/or certain of its subsidiaries will transfer all of their right, title and interest in a defined pool of receivables to the SPE. In certain transactions, the SPE may also purchase new receivables on a revolving basis as collections are received on existing receivables
- Transfer of receivables from XYZ Corp to the SPE is deemed a "true sale" for legal purposes, and is opined on as such by outside counsel
- The SPE will fund its purchases of receivables by selling or pledging interests in the receivables to an asset-backed commercial paper conduit
- The conduit funds purchases by issuing on an offering basis, in its own name, commercial paper
- XYZ Corp will have a committed source of funding from the liquidity banks should the conduit choose not, or is unable, to fund