MEMORANDUM

To: Money Market Fund Reform Proposal File

From: Adam Bolter
Senior Counsel, Division of Investment Management

Date: February 4, 2014

Re: Money Market Fund Regulation

On February 4, 2014, staff from the Division of Investment Management ("IM") and Division of Economic and Risk Analysis ("DERA") met with the representatives from the U.S. Chamber of Commerce Center for Capital Markets Competitiveness: Alice Joe and Leigh Stapleton; Boeing: Verett Mims; Airgas: Joseph Sullivan; and UPS: Gary Barth.

The following SEC staff participated in the meeting:

Diane C. Blizzard, IM
David Grim, IM
Sara Cortes, IM
Adam Bolter, IM
Kay-Mario Vobis, IM
Erin Loomis, IM
Jennifer Marietta-Westburg, DERA
Christof Stahel, DERA
Jennifer McHugh, Counsel to Chair White

Among other matters, the parties discussed the Commission's proposal on money market fund reform.

Preserve Money Market Funds

As a Cash Management Tool for American Businesses

CENTER FOR CAPITAL MARKETS
COMPETITIVENESS

February 4, 2014

Corporate Cash Management: The Fundamentals

- Business cash flows are very dynamic and variable
- Cash must be accessible to meet working capital needs
- MMFs = preferred cash management vehicle
  - As of Q3 2013, nonfinancial corporate business investors accounted for $456 billion in MMF investments. *(source: latest release of Flow of Funds)*

Key Factors:
- Liquidity
- Principal Stability
- Diversification

Benefits of MMFs

- Intraday Liquidity
- Stability of principal
- Transparency
- Investment diversification
- Built-in credit analysis
- Actively managed by (external) asset mangers

Alternatives to MMFs

	Intraday Liquidity	Stability	Diversification	Transparency	Actively Managed	Competitive Yield
Prime MMFs	Yes	Yes	Yes	Yes	Yes	Yes
Treasury MMFs	Yes	Yes	No	Yes	Yes	Yes
Bank Demand Deposit	Yes	Yes	Unknown	Limited	Unknown	No
Time Deposit	No	Yes	Unknown	Limited	Unknown	No
Offshore Funds	Yes	Yes	Yes	Yes/Limited	Yes	Yes
Custom Cash Solution	Limited	Yes/Unknown	Yes	Yes	Yes	Yes
Direct purchase of money market securities	Yes	Limited	No	Varies	No	Varies

Reform Options: Floating NAV

- ***Accounting Implications***
  - *GAAP accounting issue - cash equivalent or investment?*
  - *Bookkeeping complications*
- ***Tax* Implications**
  - IRS wash sale proposal helpful
  - Capital gains/losses still exists if it falls outside wash sale exemption
- **Operational Implications**
  - Current treasury systems are not programmed to accept floating NAV; Reprogramming estimated to cost up to $1.8M (per company) and up to 24 months to install, test and implement.
  - Investment policies need to be changed
  - Potential violation of debt covenants

The Floating NAV is unworkable.

Reform Options: Liquidity Fees & Gates

- Liquidity Fees = loss on cash investment → demonstrates poor treasury management.

- Gates = no access to cash → detrimental to business.

- Investors have limited control or visibility over fund's weekly liquidity level.

Liquidity Fees and Gates are problematic.

Reform Options: Increased Disclosure

- More frequent disclosure = better transparency.
- Shadow NAV disclosure accomplishes the same thing as a floating NAV <u>without all the accounting, tax, and operational implications</u>.

Increased disclosure helps investors understand and assess risks of investments in MMFs.

Commercial Paper Impact: Deceased Demand

- Less investment in Institutional Prime MMFs will cause demand for CP to decline.

- $74 billion in non-financial CP held by <u>taxable</u> money market funds as of October 2013. *

- Commercial Paper is the <u>most efficient and affordable</u> means of short-term financing for American businesses.

- Bank lending is a 3.5X to 10X more expensive means of financing.
    - Interest rate on CP = approx 40 bps**
    - Interest rate on LOC = approx 400 bps***

* Source: Public N-MFP data.
**varies by company.
***varies by company and based on how quickly funds needed.