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April 23, 2014

Submitted Electronically

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

RE: File No. S7-03-13—Money Market Fund Reform; Amendments to Form PF

Dear Ms. Murphy:

I. Introduction

On behalf of Wells Fargo & Company and its subsidiaries, Wells Fargo Funds Management, LLC appreciates the opportunity to comment on the analyses of money market fund-related data and economic literature conducted by the staff of the Securities and Exchange Commission's Division of Economic and Risk Analysis ("DERA") and issued on March 24, 2014 ("Analyses").[1]

As the ninth largest money market fund provider in the industry, with over $110 billion in money market fund assets under management as of March 31, 2014, we have a significant interest in the continued strength and viability of money market funds, which are an invaluable investment option for retail and institutional investors alike, and a critical source of short-term financing for American businesses, states, and municipalities. For this reason, we carefully reviewed the money market fund rule proposal issued by the Securities and Exchange

1 *See* "Liquidity Cost During Crisis Periods," DERA (March 17, 2014), available at http://www.sec.gov/comments/s7-03-13/s70313-321.pdf ("Liquidity Cost Analysis"); "Government Money Market Fund Exposure to Non-Government Securities," DERA (March 17, 2014), available at http://www.sec.gov/comments/s7-03-13/s70313-322.pdf ("Government Fund Analysis"); "Municipal Money Market Funds Exposure to Parents of Guarantors," DERA (March 17, 2014), available at http://www.sec.gov/comments/s7-03-13/s70313-323.pdf ("Guarantor Analysis"); and "Demand and Supply of Safe Assets in the Economy," DERA (March 17, 2014), available at http://www.sec.gov/comments/s7-03-13/s70313-324.pdf ("Safe Assets Analysis").

Commission ("Commission") in 2013, and submitted a detailed comment letter in response.[2] In that letter, we supported those proposals with demonstrable benefits and reasonable costs to shareholders and other stakeholders, but opposed those that fail to meet the same criteria.

Because we strongly believe a robust, informed, and objective cost-benefit analysis is critical to effective regulation, we are pleased to now have the opportunity to address certain of the Analyses.[3] While we recognize the Analyses represent the work of the staff, and not the Commission itself, we assume that these Analyses, and public comments in response, will inform Commission decision-making with respect to any final rule. In fact, each of the Analyses appears intended to support a particular regulatory outcome or conclusion. As discussed below, we believe the Analyses are inadequate to support certain of these outcomes and conclusions. In particular, we do not believe the Analyses adequately support the following: (i) ending a tax-exempt (or "municipal") money market fund's flexibility to invest up to 25% of its total assets in securities subject to guarantees or demand features of a single institution ("25% Basket"); (ii) modifying the proposed flexibility for a government money market fund to invest in non-government securities; and (iii) quelling legitimate concerns voiced in public comments on the Proposal that government money market funds may not have capacity to accept assets leaving institutional prime money market funds due to imposition of a variable net asset value ("NAV") requirement on those funds.

II. Elimination of the 25% Basket for Municipal Money Market Funds

The Commission has proposed to eliminate the 25% Basket for all money market funds, which would effectively mean that money market funds could not obtain exposure to any one guarantor above 10% of total assets. We supported the proposal, except as it applied to municipal money market funds. We opposed elimination of the 25% Basket for municipal money market funds because we believe that without it, there will be an inadequate supply of municipal securities with demand features or guarantees from appropriately high quality guarantors. As we stated in our letter, availability of guarantor support for municipal securities has substantially declined, and the market share among the top 10 support providers stood at nearly 77% at the end of 2012.[4] We fear that the elimination of the 25% Basket will require municipal funds to either close to new investment or to take on more risk through greater exposure to lower-quality guarantors.

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[2] *See* Money Market Fund Reform; Amendments to Form PF, Investment Company Act Release No. 30551 (June 5, 2013) [78 FR 36834 (June 19, 2013)] ("Proposal"); Letter from Karla M. Rabusch, Wells Fargo Funds Management, LLC, regarding the Proposal, Sept. 16, 2013 ("Comment Letter").

[3] We do not address the Liquidity Cost Analysis in this letter.

[4] Based on statistics published by *The Bond Buyer*.

The Guarantor Analysis appears intended to address these supply/credit quality concerns, first by attempting to demonstrate that municipal funds do not make significant use of the 25% Basket. To that end, the Analysis cites the fact that as of November 2012, approximately 30.6% of single state funds and 7.7% of other tax-exempt funds had exposure to at least one guarantor above 15%. In addition only 10.8% of single state funds and 2.6% of other tax-exempt funds had exposure to at least one guarantor above 20%. However, the Analysis also shows that 80.2% of single state funds and 50.0% of other tax-exempt funds (or nearly 70% of all municipal funds[5]), had exposure to at least one guarantor above 10%.

It is the data about funds that have greater than 10% exposure to at least one guarantor, rather than the data about funds that have greater than 15% and 20% exposures, that reveals the extent to which municipal funds make use of the 25% Basket. In short, it demonstrates that municipal funds, both single-state and other tax-exempt, make substantial use of the 25% Basket on a consistent basis. By way of explanation, it is important to recognize that while the 25% Basket permits exposure to a single guarantor of up to 25%, there is no requirement that any use of the Basket be confined to *one* guarantor. In fact, Rule 2a-7 under the Investment Company Act of 1940, as amended ("1940 Act"), only requires that the sum of each of a fund's exposures to individual guarantors of greater than 10% be less than or equal to 25% of total fund assets, and it is often more practical and more prudent to gain greater than 10% exposure to two of the highest quality guarantors rather than gain greater than 15% or 20% exposure to one.[6] Because the 25% Basket is the means by which any fund obtains anything greater than 10% exposure to a single guarantor, the number of funds with exposure to any one guarantor over 10% provides a reasonable estimate of the number of funds relying on the 25% Basket.

Although the Guarantor Analysis demonstrates the fact that most municipal money market funds routinely use the 25% Basket, we believe that it does not reflect the full extent of that use over time. The Analysis is hampered by the fact that the sample period (2010-2012) did not include any periods of severe stress to money market funds. The 25% Basket provides a means for portfolio managers to limit portfolio credit risk by concentrating exposure to the highest quality guarantors. While necessary during periods of relative calm, this flexibility becomes critical during more stressful periods, such as the financial crisis of 2008, when creditworthiness of all but the soundest guarantors became questionable. In essence, the 25% Basket can function as an important tool to protect money market fund investors in a crisis, and we would suggest that given the sample period, the Guarantor Analysis does not, and cannot, reflect this fact.

Beyond analyzing current reliance on the 25% Basket, the staff indicates that there should be no need for municipal funds to obtain greater than 10% exposure to any one guarantor

5 (89 single state funds + 39 other tax-exempt funds) / 189 total municipal funds = approximately 68%.

6 - *See* Rule 2a-7(c)(4)(iii)(A).

because "the credit quality of guarantors among the top twenty guarantors is similar to that of the top five guarantors suggesting that even with a 10% guarantor limit, any increase in guarantor diversification should not lead to a deterioration in guarantor credit quality."[7] We disagree with the conclusion and the staff's reasoning. First, the staff does not account for the fact that when municipal money market funds gain greater than 10% exposure to particular guarantors, it is most often to one or more of the top five guarantors. This is partly due to supply. That is, assuming just for the moment that the top 15 guarantors have similar credit quality to the top five, that does not mean that supply from the top 15 will be adequate to meet new demand due to elimination of municipal money market funds' ability to obtain greater than 10% exposure to any one of the top five guarantors.

We also respectfully disagree with the staff's contention, based on two limited factors—nationally recognized statistical ratings organization ("NRSRO") ratings and credit default swap ("CDS") spreads—that the credit quality of the top 20 guarantors is similar enough to make them interchangeable. With respect to NRSRO ratings, our collective national experience in 2008 demonstrated that these ratings are not a reliable standalone means to assess credit quality. For that reason, Congress has required the Commission to remove from its rules and regulations any reference or requirement of reliance on credit ratings for assessing the credit-worthiness of a security or money market instrument.[8] And, the Commission has subsequently removed references to credit ratings from certain of its rules and forms.[9] As a fiduciary, we cannot, and do not, rely entirely on NRSRO ratings to assess credit quality. Indeed, the data produced by the staff indicating that municipal money market funds have concentrated exposure to the top five parents of guarantors indicates that other money market fund advisers do not view the top 20 guarantors as interchangeable. Given the demonstrated limitations of NRSRO ratings, which have been recognized by lawmakers, regulators, and market participants alike, we would respectfully suggest that NRSRO ratings should not form the basis of the Commission's assessment of relative guarantor creditworthiness.

The second criteria used by the staff to assess credit quality—CDS spreads—represents one factor that money market fund advisers and portfolio managers may take into account in assessing credit quality. However, these spreads, even coupled with NRSRO ratings, are not

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7 Guarantor Analysis at 15.

8 *See* Pub. L. No. 111-203 § 939A.

9 *See, e.g.,* Removal of Certain References to Credit Ratings under the Investment Company Act, Investment Company Act Release No. 30847 (Dec. 27, 2013) [79 FR 1316 (Jan. 8, 2014)]. We note that the Commission has proposed, but has not adopted, amendments to Rule 2a-7 to remove references to credit ratings therein. *See* References to Credit Ratings in Certain Investment Company Act Rules and Forms, Investment Company Act Release No. 29592 (Mar. 3, 2011) [76 FR 12896 (Mar. 9, 2011)]. In our Comment Letter on the Proposal, we encouraged the Commission to remove references to NRSRO ratings from Rule 2a-7 at adoption due to the demonstrated limitations of NRSRO ratings.

sufficient. CDS spreads essentially represent CDS counterparties' aggregate estimates of the default risk for a particular issuer or guarantor. However, these spreads can be volatile, reflecting their tenuous nature as a measure of credit quality.[10] In the end, we do not believe that CDS spreads, even coupled with NRSRO ratings, can substitute for a careful and considered credit analysis by either portfolio managers or the Commission staff. Again, we would suggest that municipal money market fund concentration among the top five guarantors is not irrational behavior. Rather, it is based on supply and on portfolio managers' independently derived views that the top five guarantors are of higher relative credit quality than others and that gaining greater relative exposure to these guarantors reduces credit risk. We believe the Commission should not unnecessarily impede this risk-mitigating behavior, particularly based on a theory of guarantor credit quality equivalence using two limited factors.

III. Demand and Supply of Safe Assets in the Economy and Government Money Market Fund Capacity to Absorb New Assets

In response to the Commission's proposed variable NAV requirement for institutional prime money market funds, we questioned the capacity of government money market funds to accept assets migrating from institutional prime money market funds. We pointed out that supply of U.S. Government securities and repurchase agreements collateralized by U.S. Government securities has declined in recent years.[11] The Safe Assets Analysis appears intended to address concerns about government money market fund capacity to accept substantial inflows from institutional prime money market funds. However, as discussed in greater detail below, we believe that the Safe Assets Analysis misses the mark and fundamentally fails to address the capacity question. In citing an abundant supply of foreign safe assets, the Analysis does not take into account that non-U.S. safe assets are ineligible investments for both government money market funds and many other investors in domestic government securities in light of associated foreign currency risks and the typically long-dated maturities of these assets. In addition, the study does not quantify or qualitatively assess the supply of assets that must make up most or all of government money market fund portfolios—U.S. Government securities and repurchase agreements collateralized by U.S. Government securities.

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[10] For example, CDS spreads for JP Morgan reached a high of 232 bps in 2009, or nearly four times the value used in the Analysis. However, such volatility is not limited to the period of the financial crisis. CDS spreads for Bank of America reached a high of 482 bps in 2011. (Source: Bloomberg, LP)

[11] For example, the supply of repurchase agreements available to government money market funds has declined substantially in recent years. The U.S. repurchase market is reported to have shrunk 35%, from an estimated $7.02 trillion daily outstanding in the first quarter 2008 to an estimated $4.6 trillion daily outstanding in July 2013. See "Repo Market Decline Raises Alarm as Regulation Strains Debt," Bloomberg (Aug. 19, 2013), *available at* http://www.bloomberg.com/news/2013-08-19/repo-market-decline-raises-alarm-as-regulation-strains-debt-1-.html.

The Safe Assets Analysis provides statistical information and analysis about the demand and supply of "safe assets," defined as debt securities with virtually no default risk. The analysis focuses on the availability of both domestic government securities and global safe assets, rejecting the prediction of an International Monetary Fund ("IMF") report that the global economy will experience a shortfall of safe assets.[12] In discussing the potential impacts of changes to money market fund regulation, the Safe Assets Analysis correctly notes that a significant portion of prime money market fund investors could shift investments into government money market funds, increasing demand for domestic government securities and safe assets in the economy. However, it goes on to suggest that an ample supply of safe assets would meet increased demand for government securities precipitated by such a shift. Specifically, the Analysis contends that the market contains, or will contain, an adequate supply of portfolio securities necessary to allow government money market funds to absorb assets leaving institutional prime money market funds due to a potential variable NAV requirement. In support of this assertion, the Safe Assets Analysis explains that a hypothetical $357 billion shift from prime money market funds to government money market funds, based on a 20% shift, would be unlikely to create a problem given the estimated amount of $74 trillion in global safe assets.

The availability of global safe assets, regardless of their total magnitude, is simply not germane to of the question of government money market funds' ability to absorb assets shifting from prime money market funds in the event the Commission imposes a variable NAV requirement on institutional prime money market funds. As noted in footnote 25 of the Safe Assets Analysis,[13] a government money market fund must invest at least 80% of its total assets in cash, government securities as defined in section 2(a)(16) of the 1940 Act, or repurchase agreements that are collateralized with cash or government securities ("80% Test"). The 1940 Act defines a government security as "any security issued or guaranteed as to principal or interest by the United States, or by a person controlled or supervised by and acting as an instrumentality of the Government of the United States pursuant to authority granted by the Congress of the United States; or any certificate of deposit for any of the foregoing." Foreign safe assets, for example, are not eligible to satisfy a government money market funds' 80% Test.

The Safe Assets Analysis appears to be suggesting that even if foreign safe assets are not eligible to meet the 80% Test, their availability to other investors seeking greater yields may draw other investors to those opportunities, thereby ameliorating domestic government security supply concerns for government money market funds. In this vein, the analysis baldly asserts that the fungibility and substitutability of global safe assets for non-money market funds would free up the supply of domestic government securities for government money market funds absorbing assets from prime money market funds. The Analysis contains no data, analysis or

12 *See* Safe Assets Analysis at 4.

13 *See* Safe Assets Analysis at 7.

citation to other publications that supports the contention that foreign safe assets are fungible or substitutable for investors in domestic government securities. If fact, no qualitative or quantitative data is provided about the identities of other investors in domestic government securities, their past investment behaviors, legal restrictions on their investment mandates, their ability to assume associated foreign currency risks or invest in longer-dated securities or other salient characteristics. For example, accepting exposure to volatility in foreign currency exchange rates may be legally impermissible for certain investors in domestic government securities, or may present unacceptable risks because currency related losses may wipe out all, or in some cases more than all, of the income earned on foreign safe assets. In addition, other investors in government securities may be restricted to those instruments by governing documents, guidelines or other agreements. Thus, by assuming its conclusion with respect to fungibility and substitutability of global safe assets, the Safe Assets Analysis fails to affirmatively support the conclusion that the impacts of changes to money market fund regulation will be mitigated by the availability of alternative assets worldwide.

The assets that are eligible to meet a government money market fund's 80% Test constitute less that 10% of the $74 trillion figure cited in the IMF estimate of total safe assets.[14] Moreover, as noted above, the supply of short-term treasury securities, short-term federal agency securities and repurchase agreements available to government money market funds is declining due, in part, to evolving regulatory standards and other government actions. And, as noted in our previous Comment Letter, increased demand resulting from adoption of a variable NAV rule may push yields on short-term treasury securities into negative territory for a considerable time, which, in turn, may limit the ability of government money market funds to absorb assets from prime money market funds. Displaced assets from prime money market funds may instead gravitate to alternative vehicles that are less regulated than money market funds, offer less reporting and transparency, and may entail greater idiosyncratic, counter-party and non-diversification risks.

IV. Government Fund Investment in Non-Government Securities

We were pleased the Commission proposed to define "government" money market funds exempt from the proposed variable NAV requirement as money market funds that maintain at least 80% of their total assets in cash, government securities, or repurchase agreements that are collateralized fully. We believe that providing government money market funds with the flexibility to invest up to 20% in non-government Rule 2a-7-eligible securities will help to alleviate some of the issues discussed herein with respect to supply and zero or negative yields in government money market funds. However, the Government Fund Analysis appears intended to support the notion that government money market funds do not need this flexibility, even after

[14] Government money market securities total $6.82 trillion as of March 31, 2014 according to JP Morgan Securities, LLC's article "Short-Term Fixed Income" published in US Fixed Income Markets Weekly, April 4, 2014.

drastic and market-altering regulatory changes are imposed, simply because government money market funds currently do not generally invest in non-government securities up to the allowed 20% limit. While we do not dispute the accuracy of information regarding historical exposures in the sample period, it simply does not follow, as the Analysis appears to suggest, that past usage levels of non-government securities by government money market funds are indicative of future usage levels following the adoption of proposed regulatory changes, such as the imposition of a mandatory variable NAV on institutional prime money market funds.

Although many government money market funds in the sample period tended to not have an investment need to seek significant investments outside of government securities because those securities provided adequate yield and did not face supply challenges, those conditions may no longer apply in the future. While investors migrated to government money market funds during the sample period, two key differences, unique to the sample period, facilitated the supply of government securities:

- Supplies of securities from government sponsored entities ("GSEs") were not declining because GSEs were continuing their normal operations without a potential wind down of their businesses; and

- The inflows were mitigated by a significant increase in supply that absorbed a portion of the increased demand for government securities, including from the following sources:

    - $200 billion in U.S. Treasury Supplementary Financing Bills;

    - $39 billion issued by Straight-A Funding Asset Back Commercial Paper program which benefited from liquidity provided by the Federal Financing Bank and a Put Agreement from the U.S. Department of Education; and

    - The Federal Deposit Insurance Corporation's ("FDIC") Temporary Liquidity Guarantee Program which consisted of:

        - Debt Guarantee Program under which the FDIC guaranteed in full $345.8 billion in debt issued by 122 institutions, and

        - Unlimited FDIC deposit insurance under the Transaction Account Guarantee Program.

At present, not only are none of these extraordinary measures in place, but even normal levels of supply are in decline as GSEs are paying down their debt and the U.S. Treasury Department is cutting the supply of Treasury-bills in favor of longer-term notes and bonds. We believe that without the ability for government money market funds to diversify into prime and municipal securities, a significant inflow into government money market funds could force the already paltry yields on short-term government securities to turn negative. Past events in

European markets demonstrate that when money market yields turn negative, funds close to further investment. If similar events unfold in the U.S. following any regulatory changes, money market fund investors that might otherwise invest in government money market funds would be left with even more limited choices.

We believe that investors would be better served if the Commission adopts regulatory changes designed to ensure adequate disclosure of a government money market fund's investment policies.[15] The potential imposition of overly restrictive limitations on government money market funds' ability to invest in non-government securities will exacerbate the supply issues and unnecessarily restrict investor choices.

In addition, a final rule that permits government money market funds to have a modest 20% exposure to investments in non-government securities will blunt some of the potential burdens on businesses that presently depend on prime money market funds for financing needs. As monies are driven from prime money market funds to government money market funds following a potential variable NAV requirement on institutional prime money market funds, financing costs of businesses relying on prime money market funds are expected to increase substantially. The ability of government money market funds to have limited exposure to prime securities will mitigate the degree of increases in financing costs to business by buffering an otherwise massive decline in demand for those securities.

Finally, we do not believe that allowing government money market funds to invest up to 20% in non-government securities will materially increase the risks of these funds to investors or the financial system. Government money market funds that maintain 80% of their assets in government securities will have an adequate supply of liquid securities to satisfy any increased redemption pressures that a fund may face if a credit event in the 20% non-government security portion of the portfolio and/or a shift in interest rates triggers a decline in the Fund's market-based NAV. The credit quality, liquidity and maturity characteristics of a government money market fund's 80% "bucket" in government securities will enable a fund to handle significant redemption requests, even where investors believe that they have an incentive to redeem based on events affecting a government money market fund's 20% bucket in non-government securities. As such, the Proposal characterized as "minimal" the risk of government money market funds that maintain at least 80% of their total assets in cash, government securities, or repurchase agreements that are collateralized fully.[16] We agree. The Government Fund Analysis

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15 For example, if appropriate, the Commission's staff could issue interpretive guidance under Rule 35d-1 under the 1940 Act regarding the appropriateness of terms in names for government money market funds that have policies that allow for investments of up to 20% in non-government securities.

16 *See* Proposal at 67. Although we do not support the variable NAV proposal for the reasons stated in our Comment Letter, if a variable NAV rule for institutional prime money market funds is finally adopted, we would agree with the assertion stated in the Commission's proposing release

fails to provide any quantitative or qualitative assessment of the risks of non-government security holdings held by government money market funds, including with respect to any impact on the market-based NAVs of government money market funds holding non-government securities during the sample period. And therefore, it fails to refute the Commission's prior conclusion that government money market funds required to invest at least 80% in government securities pose minimal risks.

V. Conclusion

A disciplined, systematic, and objective cost-benefit analysis will play a critical role in an appropriate evaluation of the alternatives set forth in the Proposal because the impacts of any final rule will likely be far reaching and profound for all stakeholders. We applaud the efforts of the Commission's staff in recent years to define a clearer framework for producing economic analysis of costs and benefits in connection with rule proposals. The staff memorandum from the Division of Risk, Strategy, and Financial Innovation and the Office of the General Counsel entitled "Current Guidance on Economic Analysis in SEC Rulemakings" (the "Memorandum")[17] has been critical in establishing the parameters of a more rigorous analysis. In particular, the Memorandum states that the requirements for economic analysis in Commission rulemaking include, among others, the following elements: (1) the definition of a baseline against which to measure the likely economic consequences of the proposed regulation, and (2) an evaluation of the benefits and costs of the proposed action and the main alternatives identified by the analysis.[18]

At this stage of the rulemaking process, it is not entirely clear which of these elements of economic analysis each of the Analyses is seeking to satisfy. We would expect that certain of the Analyses contain data that would, in some cases, help to establish an appropriate baseline against which to measure the consequences of proposed regulation, but none of the Analyses discussed herein adequately evaluate benefits and costs of particular proposals. The Government Fund Analysis and Safe Assets Analysis are barely, if at all, probative with respect to relevant proposals. The Guarantor Analysis is relevant to the question of eliminating the 25% Basket, but the sample period is too brief and the data is misinterpreted.

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that "the benefits of retaining a stable share price money market fund option and the relative safety in a government money market fund's 80% bucket appropriately counterbalances the risks associated with the 20% portion of a government money market fund's portfolio that may be invested in securities other than cash, government securities, or repurchase agreements." *Id.*

17 *See* Memorandum at http://www.sec.gov/divisions/riskfin/rsfi_guidance_econ_analy_secrulemaking.pdf.

18 *See id* at 4.

While we do not believe that the Analyses adequately support the seemingly intended rulemaking outcomes, we appreciate that the staff has published the Analyses and sought public comments. We believe that this kind of dialogue among the staff, the Commission, and the public has the potential to facilitate better regulation through a more rigorous analysis of the costs and benefits. We look forward to continuing this dialogue in pursuit of regulatory changes that will address any remaining risk of destabilizing runs on money market funds without destroying those features that have made them such a critical investment option and source of short-term financing.

Very truly yours,

Karla M Rabusch

Karla M. Rabusch
President
Wells Fargo Funds Management, LLC