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Invested in America

April 23, 2014

VIA E-MAIL RULE-COMMENTS@SEC.GOV

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

RE: Securities Industry and Financial Markets Association comments on memoranda prepared by the staff of the Division of Economic and Risk Analysis ("DERA") of the Securities and Exchange Commission relating to File Number S7-03-13, Release No. IC-30551, *Money Market Fund Reform; Amendments to Form PF* (the "Release")

Dear Ms. Murphy:

The Securities Industry and Financial Markets Association ("SIFMA") respectfully submits these comments on four memoranda dated March 17, 2014 from the staff of DERA (the "Staff") of the Securities and Exchange Commission (the "Commission" or "SEC"), titled, respectively: Liquidity Cost During Crisis Periods (the "Liquidity Cost Memorandum");[1] Municipal Money Market Funds Exposure to Parents of Guarantors (the "Municipal MMF Memorandum");[2] Demand and Supply of Safe Assets in the Economy;[3] and Government Money Market Fund Exposure to Non-Government Securities[4] (each, a "Memorandum" and, together, the "Memoranda"). The Memoranda are intended to be informative for evaluating proposed new and amended rules and forms relating to money market funds in the Release, including Rule 2a-7 under the Investment Company Act of 1940, as amended ("Rule 2a-7"). SIFMA commented on the proposals in a letter to you dated September 17, 2013 (the "Comment Letter").[5]

This letter has been prepared by the Asset Management Group of SIFMA and the Private Client Group of SIFMA. SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. These companies are engaged in communities across the country to raise capital for businesses, promote job creation and lead economic growth. The Asset Management Group ("AMG") is SIFMA's voice for the buy-side within the securities

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1 Available at http://www.sec.gov/comments/s7-03-13/s70313-321.pdf

2 Available at http://www.sec.gov/comments/s7-03-13/s70313-323.pdf

3 Available at http://www.sec.gov/comments/s7-03-13/s70313-324.pdf

4 Available at http://www.sec.gov/comments/s7-03-13/s70313-322.pdf

5 Available at http://www.sec.gov/comments/s7-03-13/s70313-199.pdf

industry and the broader financial markets.[6] SIFMA's Private Client Group ("PCG") is composed of private wealth management professionals who are dedicated to providing personalized investment advice or trading support to retail investors.[7]

We welcome DERA's data-driven analysis of issues relating to proposed money market fund reforms and their potential costs and benefits. We appreciate the opportunity to comment regarding the insights the Memoranda offer as to money market fund reform. As further explained in this letter, we ask the Commission to consider the following relating to the Liquidity Cost Memorandum and the Municipal MMF Memorandum:

> (1) If the Commission adopts a liquidity fee, we recommend that the default level of the fee be reduced from 2% to 1%. Data in the Liquidity Cost Memorandum support that a lower default level will effectively compensate money market funds for the cost of liquidity during market turmoil.
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> (2) The Commission should not expand the credit support diversification test to 100% of the assets of a money market fund portfolio, from the current 75%. That is, money market funds should continue to be permitted to have a 25% non-diversified basket ("25% basket"). The Municipal MMF Memorandum does not show that the removal of the 25% basket is necessary and does not adequately recognize the difficulties for municipal money market funds that would result from the elimination of the 25% basket.

Below we comment on each of these two Memoranda, in turn.

(1) Liquidity Cost During Crisis Periods Memorandum

One of the Commission's proposed reforms of money market funds would impose a liquidity fee when the "Weekly liquid assets" of a money market fund (as defined in the proposed amendments to Rule 2a-7), other than a U.S. Government money market fund, are reduced to less than 15% of total assets of the money market fund. Specifically, the fund would be required to impose a liquidity fee of 2% on any redemption from the money market fund after the time the fee is imposed, unless the board finds either that such fee is not in the best interest of the money market fund or that a lower fee is in the best interest of the fund. Thus, the 2% fee is the default level for the fee, in the absence of board action.

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[6] AMG is comprised of asset management firms, including some of the largest and most influential money market fund managers in the United States, collectively, with assets under management exceeding $30 trillion. The clients of AMG member firms include, among others, registered investment companies, endowments, state and local government pension funds, private sector Employee Retirement Income Security Act of 1974 pension funds and private funds such as hedge funds and private equity funds.

[7] PCG represents wealth management professionals at global, national, regional, independent contractor, and small firms. The PCG is committed to providing proactive guidance and recommendations to enhance investor trust and confidence in the securities industry and to provide regulators and policy makers with a business perspective on legislative and regulatory proposals affecting individual investors.

In our Comment Letter, we recommended that the default level of the liquidity fee be reduced to 1%, subject to reduction by the fund's board (or to increase by the fund's board up to 2%). The reduced default level would better align the amount of the fee with the costs to the money market fund of liquidating assets to honor redemptions in times of market stress, without imposing a punitive charge on shareholders.

We believe the Liquidity Cost Memorandum supports our recommendation. DERA observed the average spread between buyer and seller initiated transactions in "Tier 1" securities and "Tier 2"[8] securities during crisis and non-crisis periods.[9] The difference between the average spread provided an estimate of the cost of obtaining liquidity during crisis periods, because spreads widen during periods of relative illiquidity.[10] According to DERA's data, the highest average weekly liquidity cost during a crisis period for securities DERA classified as Tier 1 quality was 76 basis points. The highest average weekly liquidity cost during a crisis period for securities that DERA classified as Tier 2 quality was 126.9 basis points. The differences in the average spreads between the crisis and non-crisis periods for Tier 1 and Tier 2 securities, respectively, was 51.4 basis points and 104.4 basis points.[11] Based on the figures from DERA, a 200 basis point (or 2%) liquidity fee, as proposed, would be substantially higher than necessary to compensate a money market fund for the cost of providing liquidity during a crisis period. No more than 3 percent of a money market fund portfolio may be comprised of Second Tier Securities (at the time of acquisition), so that the spread on Tier 1 securities (i.e., 51.4 basis points) is more indicative of the spread applicable to the vast majority of a money market fund portfolio and should be given commensurate weight in determining the liquidity fee as compared to the spread on Tier 2 securities. A 100 basis point (1%) default level for the liquidity fee will more closely approximate the fund's cost of providing liquidity during a crisis period for a portfolio comprised largely of Tier 1 securities.

It is important to set the default level for the liquidity fee at a level that deters redemptions in a crisis, without needlessly burdening redeeming shareholders who need access to their cash. We understand that the proposal would allow the fund board to reduce the level of the fee, but, as we described in our Comment Letter, we are concerned that the fund board may

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[8] DERA appears to refer to securities that it categorizes as the equivalent quality of First Tier Securities, as defined in Rule 2a-7, as Tier 1 securities, and to securities that it categorizes as the equivalent quality of Second Tier Securities, as defined in Rule 2a-7, as Tier 2 securities.

[9] DERA uses prices of securities reported on TRACE as the source of this data. While we agree with the ultimate findings of the Liquidity Cost Memorandum, we believe that securities reported on TRACE are not an accurate sampling of money market fund transactions. The size of the trades is far smaller than typical money market fund trades, even though the sample excludes trades less than $100,000. In addition, the securities are not of a type purchased by money market funds. Further, the maturities of the securities, even though selected to be less than 120 days remaining, are longer than a typical money market fund holding. (Money market funds are required to maintain an average weighted maturity of 60 days or less.)

[10] As DERA explained, wider spreads compensate market makers for the risk associated with holding inventory and the search costs associated with finding willing buyers. Liquidity Cost Memorandum at p. 3.

[11] Liquidity Cost Memorandum at p. 1 and p. 3.

be reluctant to reduce the fee out of fear of being second-guessed -- especially given the proposed requirement that the board disclose its analysis of a decision to reduce the fee. Also, when a fund breaches the liquidity trigger, it may be impossible to convene the board in time to change the fee from the default level before the fee initially goes into effect, so that the default fee level becomes the initial fee level before the fund board has the chance to consider the cost of liquidity.

(2) Municipal Money Market Funds Exposure to Parents of Guarantors

Under Rule 2a-7, up to 25% of a money market fund's assets (the "25% basket") may be invested in securities supported by demand features or guarantees ("credit supports") by one or more institutions (each a "credit support provider"). The remaining 75% the fund's assets must be diversified as to credit supports – that is, comprised of positions not exceeding 10% of fund assets.[12] The Commission proposes to eliminate the 25% basket, so that 100% of a fund's assets would be limited to not more than 10% per credit support provider.

Though the Municipal MMF Memorandum might seem to indicate that eliminating the 25% basket will not be problematic for money market funds, as further described below, our members believe that the ability to hold positions in excess of 10% is critical to money market funds generally, and for municipal money market funds in particular. Our members oppose elimination of the 25% basket.

The Municipal MMF Memorandum focuses on, among other things, the number of funds that utilize the 25% basket and the size of the exposure to credit supports that exceed 10%, 15% and 20% of money market fund portfolios. It suggests, for the 24 month period that DERA reviewed, that "few funds make full use of the '25% basket.'"[13] It may be the case that, for the period in question, money market funds did not utilize the 25% basket to its full extent. However, the data also show clearly that many money market funds do use the 25% basket to some extent, so eliminating it completely would appear to be punitive to funds that utilize the basket.[14] The fact that funds generally limit exposures greater than 10% or more of assets shows that funds already avoid using the 25% basket where possible, so that eliminating it will yield little additional benefit in risk reduction.

Our members do not believe that the Municipal MMF Memorandum provides sufficient basis for removing the 25% basket. Funds may in limited circumstances hold more than 20% of assets in one credit support provider according to data in this Memorandum, but funds may nevertheless make full or nearly full use of the 25% basket by holding two positions exceeding 10% in two different credit support providers. In certain circumstances, the flexibility to

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[12] Exposure to any second tier credit support provider is further limited. It must not exceed 2.5% of total assets.

[13] DERA reviewed data for the period from November 2010 through November 2012. Municipal MMF Memorandum at p. 1 and p. 11.

[14] As cited in the Comment Letter, data compiled from Crane Data and Bloomberg showed that 75% of municipal money market funds made use of the 25% basket as of June 30, 2013.

increase exposure to certain credit support providers is particularly useful for portfolio management. For example, upon downgrade of a credit support provider, a fund may need to increase exposure to other providers.

If the 25% basket is eliminated, funds will need to trim certain exposures to credit support providers. To replace those exposures, funds may be forced to add exposure to other credit support providers that they may consider to be less creditworthy (though they are still eligible under Rule 2a-7). DERA states that the quality of the top 20 providers of credit supports is similar to the quality of the top 5 providers.[15] The basis for that statement is not clear. Our members perform their own credit analysis and do not all agree on the equivalency of the quality of the top 20 credit support providers. Our members prefer (and should be permitted) to diversify in accordance with their own determinations of the quality characteristics of the available credit support providers for the benefit of their investors.

Please also consider that the effect of eliminating the 25% basket may become even more challenging under challenging economic circumstances. For example, in a deteriorating credit environment, the lack of diversification flexibility may limit the ability of municipal money market funds to manage their risk exposures as the funds bump up against an inflexible diversification limit.

As we noted in our Comment Letter, despite the Commission's assertion in the Release that there exists a broad array of first tier credit support providers,[16] it is not clear that under-utilized credit support providers will initiate or increase their support of money market eligible securities to fill the void created by increased diversification requirements. With respect to municipal money market funds, given the unique market, there has historically been a relatively narrow core group of banks and other financial institutions consistently providing much of the liquidity in the short-term municipal securities and tender option bond markets. Our members point out that the major providers of credit supports are not available in all states.[17]

As we stated in our Comment Letter, if the Commission does not retain the 25% basket, the Commission should consider other modifications to the 25% basket. For example, the Commission could permit exposure to any one or two providers of credit supports up to 15% of total assets in a fund, while still retaining the 25% basket.[18] This approach should preserve at least a portion of the necessary flexibility for managers of money market funds, while acknowledging the lack of diversity in credit support providers generally for municipal money market funds.

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[15] The Municipal MMF Memorandum states that "any increase in guarantor diversification should not lead to a deterioration in guarantor credit quality." Municipal MMF Memorandum at p. 15.

[16] See Release p. 453 et seq.

[17] For example, only a narrow group of providers issue credit supports for Ohio obligations.

[18] This approach would permit, for example, two credit support providers each of which supports up to 12.5% of assets.

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SIFMA respectfully urges the Commission to consider our comments, in order to make the best use of the data in the Memoranda. Money market funds are essential to a well-functioning financial system, and we hope any reforms will strengthen them and preserve their benefits.

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If you have any questions or require additional information, please do not hesitate to contact Tim Cameron of AMG at 212-313-1389, Matt Nevins of AMG at 212-313-1176, John Maurello of PCG at 212-313-1241 or Joan Swirsky of Stradley at 215-564-8015. Thank you for your attention to these comments.

Sincerely,

Timothy W. Cameron
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SIFMA Asset Management Group - Head

John Maurello
Managing Director
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Matthew J. Nevins
Managing Director and Associate General Counsel
SIFMA Asset Management Group

cc: The Honorable Mary Jo White
The Honorable Daniel M. Gallagher
The Honorable Kara M. Stein
The Honorable Luis A. Aguilar
The Honorable Michael S. Piwowar
Norm Champ, Director, Division of Investment Management