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April 21, 2014

Elizabeth M. Murphy
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

RE: Money Market Fund Reform; Release No. S7-03-13

Dear Ms. Murphy:

Enclosed for filing in the above referenced comment docket on money market fund reform is a copy of a submission we made to the Board of Governors of the Federal Reserve System on behalf of Federated Investors, Inc. concerning the eligibility of certain money market funds as highly liquid assets under the Board's Regulation YY. This submission highlights the liquidity characteristics of money market funds.

Sincerely,

Melanie L. Fein

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Raymond Natter

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Enclosure

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April 9, 2014

Robert deV. Frierson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551

Re: Regulation YY—Request for Determination that Federated U.S. Treasury Cash Reserves, Federated Treasury Obligations Fund, and Federated Government Obligation Fund are Highly Liquid Assets

Dear Mr. Frierson:

We are writing on behalf of Federated Investors, Inc. to request a determination by the Board of Governors that shares of the following money market funds sponsored and advised by Federated Investors, Inc. are "highly liquid assets" for purposes of the liquidity buffer required to be maintained by large bank holding companies and foreign banking organizations with U.S. operations under sections 252.35(b) and 252.157(c) of Regulation YY:

> Federated U.S. Treasury Cash Reserves which holds only U.S. Treasury securities;
>
> Federated Treasury Obligations Fund which holds only U.S. Treasury securities and repurchase agreements collateralized by such securities; and
>
> Federated Government Obligations Fund which holds only U.S. Treasury securities, securities issued or guaranteed by U.S. government agencies and government-sponsored enterprises, and repurchase agreements collateralized by such securities.

The Funds are managed by Federated Investors, Inc., one of the largest investment managers in the United States with $376.1 billion in assets under management as of December 31, 2013.

The enclosed memorandum demonstrates how the Funds satisfy the purposes and requirements of the liquidity buffer in Regulation YY. It shows that, because of the Funds' essential features and regulation under the Investment Company Act of 1940, shares of the Funds are among the most highly liquid of assets available in the financial marketplace. It shows that the shares are treated as cash equivalents under generally accepted accounting principles and as highly liquid for a variety of regulatory purposes. Finally, it shows that the Funds are as liquid if not *more* liquid than many of the other instruments contemplated as highly liquid assets under Regulation YY.

Regulation YY contemplates that a covered company will demonstrate to the Board's satisfaction that a particular asset is "highly liquid" for purposes of the liquidity buffer. The regulation does not preclude such a determination based on information provided by the issuer of the asset. We believe a Board determination with respect to the Funds is appropriate in order to broaden the types of liquid assets eligible to be included in the liquidity buffer and to facilitate compliance with the regulation.

Based on the information and analysis in the attached memorandum, we respectfully request a determination by the Board that shares of the Funds are "highly liquid assets" eligible to be included in a covered company's liquidity buffer for purposes of Regulation YY. We also request the opportunity to meet with the Board's staff to discuss this matter.

Sincerely,

Melanie L. Fein

Melanie L. Fein

Raymond Natter

Raymond Natter

Enclosure

cc: Scott G. Alvarez, General Counsel
Legal Division

Lauri Schaffer, Associate General Counsel
Legal Division

Mark E. Van Der Weide, Senior Associate Director
Division of Banking Supervision and Regulation

Memorandum in Support of Request for Determination that Certain Federated Money Market Funds are Highly Liquid Assets for Purposes of the Regulation YY Liquidity Buffer Requirement

I. INTRODUCTION

The Board of Governors on February 18, 2014, adopted amendments to Regulation YY that establish enhanced prudential standards for bank holding companies with consolidated assets of $50 billion or more and foreign banking organizations with combined U.S. assets of $50 billion or more (referred to herein as "covered companies") pursuant to Section 165 of the Dodd-Frank Act.[1] Among other things, the amended regulation at 12 C.F.R. §§ 252.35(b) and 252.157(c) requires such companies to maintain a buffer of unencumbered "highly liquid assets." The regulation defines such assets to include cash, U.S. government and agency securities, and "any other asset" that a covered company demonstrates to the satisfaction of the Board meets certain liquidity requirements.

This memorandum is submitted in support of a request for a determination by the Board that shares of the following money market funds qualify as "highly liquid assets" for purposes of the liquidity buffer requirement in sections 252.35(b) and sections 252.157(c) of Regulation YY:

> Federated U.S. Treasury Cash Reserves which holds only U.S. Treasury securities;
>
> Federated Treasury Obligations Fund which holds only U.S. Treasury securities and repurchase agreements collateralized by such securities; and
>
> Federated Government Obligations Fund which holds only U.S. Treasury securities, securities issued or guaranteed by U.S. government agencies and U.S. government-sponsored enterprises, and repurchase agreements collateralized by such securities.

II. THE REGULATION YY LIQUIDITY BUFFER

Regulation YY, as amended, requires each covered company to maintain a liquidity buffer sufficient to meet its projected net cash-flow needs over a 30-day period under different stress scenarios, effective June 1, 2014.[2] The liquidity buffer must consist of highly liquid assets that are unencumbered.

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[1] 79 Fed. Reg. 17240 (March 27, 2014).

[2] 12 C.F.R. § 252.35(b) (U.S. bank holding companies with total consolidated assets of $50 billion or more) and § 252.157(c) (foreign banking organizations with combined U.S. assets of $50 billion or more).

A. Definition of "Highly Liquid Asset"

A "highly liquid asset" is defined in Regulation YY to include:

- Cash;
- Securities issued or guaranteed by the United States, a U.S. government agency, or a U.S. government-sponsored enterprise; or
- Any other asset that the company demonstrates to the satisfaction of the Board:

(1) Has low credit risk and low market risk;

(2) Is traded in an active secondary two-way market that has committed market makers and independent bona fide offers to buy and sell so that a price reasonably related to the last sales price or current bona fide competitive bid and offer quotations can be determined within one day and settled at that price within a reasonable time period conforming with trade custom; and

(3) Is a type of asset that investors historically have purchased in periods of financial market distress during which market liquidity has been impaired.[3]

A highly liquid asset must be unencumbered in order to qualify for the liquidity buffer in Regulation YY. An asset is defined as "unencumbered" if it:

- Is free of legal, regulatory, contractual, or other restrictions on the ability of the company promptly to liquidate, sell or transfer the asset; and
- Is either: (1) not pledged or used to secure or provide credit enhancement to any transaction; or (2) pledged to a central bank or a U.S. government-sponsored enterprise, to the extent potential credit secured by the asset is not currently extended by such central bank or U.S. government-sponsored enterprise or any of its consolidated subsidiaries.[4]

[3] 12 C.F.R. §§ 252.35(b)(3)(i) and 252.157(c)(7)(i).
[4] 12 C.F.R. §§ 252.35(b)(3)(ii) and 252.157(c)(7)(ii).

In calculating the amount of a highly liquid asset included in the liquidity buffer, a covered company must discount the fair market value of the asset to reflect any credit risk and market price volatility of the asset.[5]

Regulation YY imposes a diversification requirement under which the liquidity buffer must not contain significant concentrations of highly liquid assets by issuer, business sector, region, or other factor related to the company's risk, except with respect to cash and securities issued or guaranteed by the United States, a U.S. government agency, or a U.S. government-sponsored enterprise.[6]

B. "Other" Highly Liquid Assets

As noted, the definition of highly liquid asset includes "other" assets besides cash and U.S. government securities that meet certain liquidity requirements. The Board must determine that such assets have low credit and market risk and the ability to settle trades at a reasonably ascertainable price, and are a type of asset that investors historically have purchased in periods of financial market distress when market liquidity has been impaired.

In the *Federal Register* notice accompanying the final regulation, the Board stated that "liquidity characteristics of assets may vary under different types of stress scenarios" and that the regulation affords each company discretion to determine whether an asset would be liquid under a particular scenario.[7] The Board emphasized that the regulation is not intended to restrict qualifying assets to cash and government securities:

> The Board also believes that restricting the assets available for liquidity coverage to cash and securities issued or guaranteed by the United States, a U.S. government agency, or a U.S. government-sponsored enterprise is unnecessarily limited, and could have negative effects on market liquidity generally. As a result, consistent with the proposal, the final rule defines highly liquid assets to include cash, securities issued or guaranteed by the United States, a U.S. government agency, or a U.S. government-sponsored enterprise, and any other asset that a bank holding company demonstrates to the satisfaction of the Board meets defined characteristics of liquidity.[8]

[5] 12 C.F.R. §§ 252.35(b)(3)(iii) and 252.157(c)(7)(iii).
[6] 12 C.F.R. §§ 252.35(b)(3)(iv) and 252.157(c)(7)(iv).
[7] 79 Fed. Reg. at 17259.
[8] 79 Fed. Reg. at 17259.

The Board stated that it was responding to public comments on the proposed regulation by broadening the types of assets that may be deemed "highly liquid":

> The commenters asked the Board to revise the definition of highly liquid assets specifically to enumerate a broader scope of assets, such as foreign sovereign obligations and obligations issued by multi-lateral development and central banks; claims against central banks of acceptable sovereign issuers; gold; FHLB borrowing capacity; committed lines of credit; inventory positions (including equities) maintained by the broker-dealer operations of a bank holding company, if any; municipal securities; **shares of money market mutual funds holding U.S. government securities**; and collateral accepted by the discount window. . . .[9]

The Board stated that "other" highly liquid assets generally would include assets that qualify as "high-quality liquid assets" under the pending proposed Basel III Liquidity Coverage Ratio ("LCR"), assuming the other requirements of the regulation are met.[10] The Board stated that such assets generally would qualify as liquid for purposes of the Regulation YY liquidity buffer:

> Assets that are high-quality liquid assets under the proposed U.S. LCR (which include equities included in the S&P 500 index or comparable indices and investment grade corporate bonds) would be liquid under most scenarios; however, the bank holding company would be required to make the demonstration to the Board required by the final rule, meet the diversification requirement … and ensure that the inclusion of these assets in the buffer would be appropriate taking into consideration the liquidity risk profile of the company….[11]

Assets that are high quality liquid assets under the proposed LCR include:

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[9] *Id.* (emphasis added)

[10] See Liquidity Coverage Ratio: Liquidity Risk Measurement, Standards, and Monitoring, 78 Fed. Reg. 71818 (Nov. 29, 2013). The proposed LCR would require internationally active banking organizations and nonbank financial companies supervised by the Board to hold an amount of high-quality liquid assets sufficient to meet expected net cash outflows under a supervisory stress scenario over a 30-day time horizon. The Board stated that the proposed LCR and the Regulation YY liquidity buffer are designed to complement one another.

[11] 79 Fed. Reg. at 17259.

- Foreign sovereign debt securities that meet certain requirements;
- Publicly traded corporate debt securities that are investment grade and a reliable source of liquidity during stressed market conditions as demonstrated by the market price of the security declining by no more than 20 percent during a 30 calendar-day period of significant stress;
- Equity securities included in the Standard & Poor's 500 Index issued by an entity whose publicly traded common equity shares have a proven record as a reliable source of liquidity during stressed market conditions as demonstrated by the market price of the security declining by no more than 40 percent during a 30 calendar-day period of significant stress.[12]

Accordingly, Regulation YY contemplates that the above assets are presumed to be treated as highly liquid for purposes of the liquidity buffer, assuming the other requirements of the regulation are met.

III. THE FEDERATED FUNDS

A. Basic Fund Features

Federated U.S. Treasury Cash Reserves, Federated Treasury Obligations Fund, and Federated Government Obligations Fund (collectively, the "Funds") are investment companies registered with the Securities and Exchange Commission that operate as a money market funds ("MMFs") subject to SEC Rule 2a-7 pursuant to the Investment Company Act of 1940. The Funds' investment objective is to provide current income consistent with stability of principal. A copy of the prospectus for each Fund is attached hereto.

As money market funds, the Funds seek to maintain a stable net asset value (NAV) of $1.00 per share. The Funds have never failed to pay redeeming shareholders less than $1.00 per share. The Funds offer same-day availability of redemption proceeds to shareholders who redeem their shares in accordance with the Fund's procedures.

Each Fund's portfolio consists solely of categories of securities, or repurchase agreements collateralized by such securities, that are defined as "highly liquid" under Regulation YY. Under SEC rules, each Fund must notify

[12] 78 Fed. Reg. 71818, 71860 (Nov. 29, 2013).

shareholders at least 60 days in advance of any change in its investment policies that would enable the Fund to invest less than 80 percent of its net assets in U.S. government investments. The Funds do not invest in commercial paper, bank certificates of deposit, or foreign securities.

Each Fund has been accepted by the Federal Reserve Bank of New York as a counterparty in the Reserve Bank's reverse repurchase agreement program.

1. Federated U.S. Treasury Cash Reserves

Federated U.S. Treasury Cash Reserves holds only the following:

- Short-term U.S. Treasury bills and notes.

As of February 28, 2014, the Fund had $20.4 billion in net assets with a weighted average maturity of 59 days and a weighted average life of 61 days. As of January 31, 2014, the Fund had daily liquidity of 99.48 percent and weekly liquidity of 99.48 percent. The Fund has existed since June 11, 1991 and is rated AAAm by Standard & Poor's and Aaa-mf by Moody's, which are the highest credit ratings given by these rating agencies for money market funds.

2. Federated Treasury Obligations Fund

Federated Treasury Obligations Fund holds only the following:

- Short-term U.S. Treasury bills and notes, and
- Repurchase agreements collateralized by U.S. Treasury securities.

As of February 14, 2014, the Fund had approximately $25 billion in net assets, of which approximately $16 billion (63 percent) was in U.S. Treasury bills and notes and $9 billion (37 percent) was in repurchase agreements collateralized by such securities. As of February 14, 2014, the weighted average maturity of the Fund was 42 days and the weighted average life was 42 days. As of February 28, 2014, the Fund had daily liquidity of 77.01 percent and weekly liquidity of 99.83 percent. This Fund has existed since December 12, 1989 and is rated AAAm by Standard & Poor's and Aaa-mf by Moody's.

3. Federated Government Obligations Fund

Federated Government Obligations Fund holds only the following:

- Short-term U.S. Treasury notes,

- Securities issued or guaranteed by U.S. government agencies or U.S. government-sponsored enterprises ("GSEs"), and
- Repurchase agreements collateralized by securities issued or guaranteed by the U.S. Treasury, U.S. government agencies or GSEs.[13]

As of March 14, 2014, the Fund had approximately $32 billion in net assets, of which approximately 3.5 percent was in U.S. Treasury notes, 44.7 percent was in U.S. government agency and GSE securities, and 51.8 percent was in repurchase agreements collateralized by such securities. As of February 28, 2014, the weighted average maturity of the Fund was 42 days and the weighted average life was 89 days.

As of February 28, 2014, the Fund had daily liquidity of 38.06 percent and weekly liquidity of 67.43 percent. This Fund has existed since March 30, 1990 and is rated AAAm by Standard & Poor's, Aaa-mf by Moody's, and AAAmmf by Fitch.

B. Fund Investment Adviser

Each Fund is advised by Federated Investment Management Company, an investment adviser registered under the Investment Advisers Act of 1940 that is a wholly-owned subsidiary of Federated Investors, Inc. Federated has been in the investment management business since 1955 and is one of the largest investment managers in the United States. As of December 31, 2013, Federated had $376.1 billion in assets under management, of which $240 billion was held by 47 money market funds.

All of the MMFs advised by Federated have an NAV of $1.00 per share. No MMF advised by Federated Investors, Inc. or its affiliates has ever failed to pay redeeming shareholders less than $1.00 per share.

C. Regulation under Investment Company Act

As registered MMFs, the Funds are highly regulated under the Investment Company Act of 1940 and Rule 2a-7 of the Securities and Exchange Commission thereunder.[14] The Rule imposes stringent credit quality, liquidity, diversification,

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[13] GSEs include the Federal Home Loan Bank System, Federal Home Loan Mortgage Corporation ("Freddie Mac"), Federal National Mortgage Association ("Fannie Mae"), Government National Mortgage Association ("Ginnie Mae"), and Farm Credit System.

[14] 17 C.F.R. § 270.2a-7.

transparency, stress testing, and other requirements on MMFs. These requirements are summarized in the Appendix hereto.

Among other things, Rule 2a-7 requires each Fund to maintain a weighted average portfolio maturity of 60 days or less. The Rule imposes a 10 percent daily and 30 percent weekly liquidity requirement—that is, each Fund must be able to liquidate 10 percent of its portfolio assets within one day and 30 percent within five business days. As noted above, the Funds more than meet these liquidity requirements.

D. Experience During the Financial Crisis

During the 2007-2009 financial crisis, each of the Funds maintained a net asset value of $1.00 per share. The market-value or "shadow" NAV of each fund deviated less than five basis points (i.e., less than $0.0005) below $1.00.

Each Fund gained assets during the crisis as investors sought safety and liquidity. During the period from September 2, 2008 to December 31, 2008:

> Federated U.S. Treasury Cash Reserves gained $35.7 billion or 253 percent in assets;
>
> Federated Treasury Obligations Fund gained $8.9 billion or 35.6 percent in assets; and
>
> Federated Government Obligations Fund gained $27.5 billion or 91.5 percent in assets.

During the period from September 2, 2008 to October 7, 2008:

> Federated U.S. Treasury Cash Reserves increased from $14.1 billion to $36.1 billion in assets;
>
> Federated Treasury Obligations Fund increased from $25 billion to $34.5 billion in assets; and
>
> Federated Government Obligations Fund increased from $30 billion to $39.9 billion.

IV. THE FUNDS ARE HIGHLY LIQUID FOR MANY REGULATORY PURPOSES

A. The Funds are Treated as Cash Equivalents by FASB

Money market funds are treated as the equivalent of cash under accounting standards codified by the Financial Accounting Standards Board ("FASB").

FASB Codification 305-10-20 (and its predecessor FASB Statement of Financial Accounting Standards No. 95) requires a business entity that publishes financial statements to provide a statement of cash flows for each relevant period of operations. The statement of cash flows is required to explain the change during the period in cash and cash equivalents. The purpose of a statement of cash flows is, among other things, to help creditors and investors assess the entity's ability to meet its obligations.

For purposes of FASB Codification 305-10-20, "cash" includes "demand deposits with banks or other financial institutions":

> Consistent with common usage, cash includes not only currency on hand but demand deposits with banks or other financial institutions. Cash also includes other kinds of accounts that have the general characteristics of demand deposits in that the customer may deposit additional funds at any time and also effectively may withdraw funds at any time without prior notice or penalty.[15]

No distinction is made between insured and uninsured demand deposits in FASB Codification 305-10-20.

A "cash equivalent" is defined by FASB Codification 305-10-20 to include Treasury bills and money market funds:

> Cash equivalents are short-term, highly liquid investments that have both of the following characteristics:
>
> a. readily convertible to known amounts of cash;
>
> b. So near their maturity that they present insignificant risk of changes in value because of changes in interest rates.

[15] FASB Accounting Standards Codification 305-10-20, definition of "cash equivalent" in Glossary. See also FASB Statement of Financial Accounting Standards No. 95, n. 1 (same definition).

> Generally, only investments with original maturities of three months or less qualify under that definition. . . . Examples of items commonly considered to be cash equivalents are Treasury bills, commercial paper, **money market funds**, and federal funds sold (for an entity with banking operations).[16]

B. The Funds are Cash Equivalents under the Investment Company Act

The SEC has stated that MMFs "often serve as a substitute for checking accounts and provide an important vehicle for cash management for individual investors as well as many institutions and businesses."[17]

The SEC staff has determined that MMF shares may be treated as "cash items" for purposes of determining whether an issuer is an investment company as defined in section 3(a)(1)(C) of the Investment Company Act of 1940 and rule 3a-l thereunder.[18] The staff stated:

> Money market fund shares generally are equivalent to cash items. . . . As stated above, the term "cash item" is not defined in the text of the Investment Company Act, or in rule 3a-l. In proposing rule 3a-l, however, the Commission set forth the following list of what would be considered to be cash items for purposes of the rule: cash, coins, paper currency, demand deposits with banks, timely checks of others, cashier checks, certified checks, bank drafts, money orders, travelers checks, and letters of credit. This list illustrates what we believe to be the essential qualities of a cash item for purposes of section 3(a)(1)(C) and rule 3a-l—a high degree of liquidity and relative safety of principal. In our view, money market fund shares have these same qualities because of the specific regulatory requirements with which money market funds must comply.[19]

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[16] FASB Accounting Standards Codification 305-10-20, definition of "cash equivalent" in Glossary (emphasis added). See also FASB Statement of Financial Accounting Standards No. 95, §§ 8 and 9 (same definition).

[17] See Investment Company Act Rel. No. 24082 (Oct. 14, 1999), text accompanying n.6; Investment Company Act Rel. No. 21216 (July 19, 1995).

[18] See Willkie Farr & Gallagher No-Action Letter, 2000 SEC No-Act. LEXIS 916 (Oct. 23, 2000) (an issuer may treat money market fund shares as "cash items" and not as investment securities for purposes of determining whether the issuer is an investment company).

[19] *Id*.

The staff stated that investors view MMFs "as an alternative to bank deposits and checking accounts, even though money market funds lack federal deposit insurance and there is no guarantee that the funds will maintain a stable NAV."[20]

C. The Funds are Cash Equivalents under Regulation T

Money market funds are treated as cash equivalents for purposes of the Board's Regulation T, which regulates extensions of credit by securities brokers and dealers. The regulation defines "cash equivalent" to include MMFs:

> Cash equivalent means securities issued or guaranteed by the United States or its agencies, negotiable bank certificates of deposit, bankers acceptances issued by banking institutions in the United States and payable in the United States, or money market mutual funds.[21]

D. The Funds are Permissible Investments for Banks

The Comptroller of the Currency has interpreted the Glass-Steagall Act to permit national banks to purchase for their own accounts shares of mutual funds that invest solely in securities that a national bank may purchase directly.[22] Mutual funds that enter into repurchase agreements collateralized by permissible securities are permitted bank investments.[23] No limitation is imposed on the amount of the bank's investment if the fund's portfolio consists solely of securities in which the bank could invest directly without limitation pursuant to 12 U.S.C. §24(Seventh), including repurchase agreements on such securities.

Because the portfolios of the Funds consist entirely of U.S. Treasury, U.S. government agency, and GSE securities, and repurchase agreements collateralized by such securities—all of which are permissible investments for a national bank without limitation—each of the Funds is a permissible investment for such a bank

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[20] *Id*. ("As with bank deposits and checking accounts, investments in money market funds permit an issuer to maintain ready cash reserves for use in meeting its business expenses.").

[21] See 12 CFR § 220.2 (Credit by Brokers and Dealers).

[22] OCC Banking Bulletin BC-220 (Nov. 21, 1986).

[23] See Office of the Comptroller of the Currency, Comptroller's Handbook—Investment Securities, at 5 ("A bank's investment in shares of investment companies that use futures, forward placement and options contracts, repurchase agreements, and securities lending arrangements as part of their portfolio management strategies is permitted, provided that those instruments would be considered acceptable for use in a national bank's own investment portfolio."). The OCC generally views repurchase agreements as borrowings rather than as securities subject to restrictions on investments.

without limitation.[24] The Funds similarly are permissible investments for state banks.[25]

E. The Funds are Eligible Brokerage Cash Sweep Vehicles

MMFs are eligible investments for free credit balances held by broker-dealers under SEC rules pertaining to the safety of customer funds. Free credit balances are funds payable by a broker-dealer to its customers on demand resulting from cash deposited by the customer to purchase securities, proceeds from the sale of securities or other assets in the customer's account, or earnings from dividends and interest on securities and other assets held in the customer's account.[26]

Broker-dealers routinely transfer or "sweep" free credit balances to either MMFs or bank deposits, which are the only permitted sweep investments for such funds under SEC rules.[27] In amending its rules recently to facilitate such sweeps, the SEC stated:

> Sweep programs provide a mechanism for excess cash in a customer's securities account to be held in a manner that allows the customer to earn interest on the funds but retain the flexibility to quickly access that cash to purchase securities or withdraw it. In effect, transferring this excess cash to a bank account or money market fund is an alternative to retaining a credit balance in the customer's securities account. The final rule is designed to accommodate this alternative by providing broker-dealers with flexibility in the operation of sweep programs. The Commission believes it is appropriate to confine this

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[24] Comptroller's Handbook—Investment Securities, at 6-7.

[25] See 12 U.S.C. § 1831a; 12 C.F.R. § 208.21(b).

[26] Under SEC Rule 15c3-3, "The term free credit balances liabilities of a broker or dealer to customers which are subject to immediate cash payment to customers on demand, whether resulting from sales of securities, dividends, interest, deposits or otherwise. . . ." 17 C.F.R. § 240.15c3–3(a)(8).

[27] Rule 15c3–3(a)(17) states: "The term Sweep Program means a service provided by a broker or dealer where it offers to its customers the option to automatically transfer free credit balances in the securities account of the customer to either a money market mutual fund product as described in [Rule 2a–7] or an account at a bank whose deposits are insured by the Federal Deposit Insurance Corporation." 17 C.F.R. § 240.15c3–3(a)(17).

> flexibility to products that approximate the holding of a customer's excess cash in a securities account.[28]

F. The Funds are Eligible Investments for FCMs and DCOs

The Funds also are permissible investments for segregated customer funds of futures commission merchants ("FCMs") and derivatives clearing organizations ("DCOs"). Under rules of the Commodity Futures Trading Commission, FCMs and DCOs must invest such funds in a manner that minimizes exposure to credit, liquidity, and market risks both to preserve their availability to customers and to enable investments to be quickly converted to cash at a predictable value in order to avoid systemic risk. Rule 1.25 of the CFTC requires that such investments "must be 'highly liquid' such that they have the ability to be converted into cash within one business day without material discount in value."[29]

Under the rule, an FCM or DCO generally may invest all of its segregated funds in money market funds subject to certain asset-based concentration limits. There is no concentration limit for investments in MMFs whose portfolios consist solely of obligations of the United States and obligations fully guaranteed as to principal and interest by the United States.[30]

In 2011, the CFTC revised the types of investments an FCM or DCO may make with customer funds under section 1.25. Among other things, the amendments *removed* from the list of permitted investments corporate debt obligations not guaranteed by the U.S. government, foreign sovereign debt, and in-house and affiliate transactions—investments that Regulation YY contemplates would be "highly liquid assets."[31]

G. The Funds are Permissible Investments for Bank Trust Cash

Bank trust departments commonly use money market funds as investments for cash in their trust accounts, often through sweep arrangements. Under rules of the Office of the Comptroller of the Currency, trust funds awaiting investment

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[28] 78 Fed. Reg. 51824, 51839 (Aug. 21, 2013). The SEC noted that "the disclosed terms of most sweep programs allow the money market fund or bank up to seven days to meet requests for withdrawals." *Id.* at 51841.

[29] 7 C.F.R. § 1.25(b)(1).

[30] A 50 percent concentration limit applies to investments in other MMFs. Additionally, FCMs and DCOs investing in other MMFs may invest no more than 25 percent in one family of funds and no more than ten percent in any individual MMF.

[31] Under revised section 1.25, an FCM or DCO may invest in MMFs that invest in commercial paper, subject to the limitations in the regulation.

may not remain uninvested or undistributed any longer than reasonable for the proper management of the account and consistent with applicable law.[32]

A bank may deposit trust account cash in its own deposits, provided the bank sets aside collateral for uninsured deposits. Acceptable collateral includes direct obligations of the United States, obligations fully guaranteed by the United States, securities that are eligible for investment by national banks (including money market funds), and readily marketable securities of the types permitted under state trust law.[33]

MMFs also are permissible investments for collective funds maintained by banks for the administration of their trust accounts, including short-term investment funds (STIFs).[34]

H. The Funds are "Money" for Monetary Policy Purposes

The Board measures the supply of money in the economy on an ongoing basis as a tool of monetary policy.[35] Money market funds are treated as "money" for this purpose and are part of the "money stock" or "monetary base." The Board's monetary aggregates are defined as M1 (generally including currency in circulation, demand deposits, and NOW accounts) and M2 (generally including M1 plus non-retirement balances in savings deposits, money market deposits, small-denomination time deposits, and retail money market funds).[36] The Board has described the monetary aggregates as follows:

> The first, M1, is made up of types of money commonly used for payment, basically currency and checking deposits. The second, M2, includes M1 plus balances that generally are similar to transaction accounts and that, for the most part, can be converted fairly readily to M1 with little or no loss of principal.[37]

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[32] 12 C.F.R. § 9.10.
[33] *Id.*
[34] 12 C.F.R. § 9.18.
[35] See generally Ben Bernanke, Monetary Aggregates and Monetary Policy at the Federal Reserve: A Historical Perspective, Speech dated Nov. 10, 2006 ("In an amendment to the Federal Reserve Act in 1977, the Congress formalized the Federal Reserve's reporting of monetary targets by directing the Board to 'maintain long run growth of monetary and credit aggregates … so as to promote effectively the goals of maximum employment, stable prices, and moderate long-term interest rates.')".
[36] See Federal Reserve Statistical Release H.6, Money Stock Measures.
[37] Federal Reserve Board, Purposes and Functions, at 22.

The inclusion of MMFs in the monetary aggregates reflects the highly liquid nature of these money market instruments.

MMFs also are grouped with checkable deposits and currency in the Federal Reserve's "Flow of Funds" statistical tables which are used for monetary policy purposes.[38]

I. The Funds are "Safe Assets"

As money market funds, the Funds are considered by economists to be "safe assets" along with bank deposits and Treasury securities:

> Our definition of "safe" assets includes assets that are either directly or indirectly used in an information-insensitive fashion, i.e. as money. The key components of "safe" debt include bank deposits, **money market mutual fund shares**, commercial paper, federal funds and repurchase agreements ("repo"), short-term interbank loans, Treasuries, agency debt, municipal bonds, securitized debt, and high-grade financial-sector corporate debt.[39]

As safe assets, MMFs facilitate economic activity and serve a variety of financial purposes:

> Safe assets are used as a reliable store of value and aid capital preservation in portfolio construction. They are a key source of liquid, stable collateral in private and central bank repurchase (repo) agreements and in derivatives markets, acting as the "lubricant" or substitute of trust in financial transactions. As key components of prudential regulations, safe assets provide banks with a mechanism for enhancing their capital and liquidity buffers. As benchmarks, safe assets support the pricing of other riskier

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[38] See Federal Reserve Statistical Release, Z.1, Financial Accounts of the United States, Flow of Funds, Balance Sheets, and Integrated Macroeconomic Accounts, Fourth Quarter 2013. See, e.g., tables F.115, Life Insurance Companies, L.114 Property-Casualty Insurance Companies, B.100 Balance Sheet of Households and Nonprofit Organizations, F.100.a Nonprofit Organizations.

[39] Gary Gorton, Stefan Lewellen, and Andrew Metrick, May 2012, "The Safe Asset Share," American Economic Review: Papers and Proceedings, 102(3), at 4 (emphasis added).

> assets. Finally, safe assets have been a critical component of monetary policy operations.[40]

V. THE FUNDS SHOULD BE DEEMED HIGHLY LIQUID UNDER REGULATION YY

A. The Funds are More Liquid than Some Treasury Holdings

As noted, Regulation YY defines a "highly liquid asset" to include cash and securities issued or guaranteed by the United States, a U.S. government agency, or a U.S. government-sponsored enterprise. The Funds consist solely of such securities and, in the case of Federated Treasury Obligations Fund and Federated Government Obligations Fund, repurchase agreements backed by such securities.

Purchasers of Fund shares acquire the right to a proportional interest in the Funds' underlying securities. Upon liquidation, the Funds' shareholders are entitled to an in-kind distribution of the Funds' assets. The Funds are essentially pass-through vehicles, as the Board's Regulation D recognizes:

> A purchaser of shares of a MMMF obtains an interest in a pro rata portion of the assets that comprise the MMMF's portfolio.[41]

With respect to repurchase agreements, Regulation D states:

> Accordingly, regardless of whether the repurchase agreement involves United States government or agency obligations directly or shares in a MMMF whose portfolio consists entirely of United States government or agency obligations, an equitable and undivided interest in United States and agency government obligations is being transferred.[42]

The Funds may be more liquid than a portfolio of directly held U.S. government securities in stress scenarios. The Funds always pay redeeming shareholders $1.00 per share at par on the date of redemption. Each Fund's portfolio is professionally managed to hold securities to maturity while

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[40] *Id.*

[41] 12 C.F.R. § 204.124.

[42] 12 C.F.R. § 204.124 (Repurchase agreement involving shares of a money market mutual fund whose portfolio consists wholly of United States Treasury and Federal agency securities).

maintaining a sufficiently short-term average maturity to be able to pay redeeming shareholders $1.00 per share.[43] In contrast, a bank holding company that directly holds a portfolio of U.S. government securities of different maturities may need to sell such securities at a discount in the event it needs to liquidate the securities for cash. Thus, the realized value of the company's portfolio of U.S. government securities may be less than the value of identical securities held through the Funds.

It is noteworthy that, whereas the Funds have maintained the highest possible credit rating in their asset category, at least one credit rating agency has downgraded U.S. government securities.[44] The downgrade reflects reduced confidence in the government's ability to manage its finances.

B. The Funds are More Liquid than Some Forms of Cash

The Funds are treated as cash equivalents for a variety of purposes, as described above, and are *more* liquid than certain forms of cash.

The term "cash" is not defined in Regulation YY. "Cash" generally is understood to include bank demand deposits and transaction accounts (i.e., checking accounts).[45] Although the terms "demand deposit" and "transaction account" are not defined in Regulation YY, these terms are defined in the Board's Regulation D pertaining to reserve requirements.[46]

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[43] As noted, the Funds are subject to SEC rules that impose a 10 percent daily and 30 percent weekly liquidity requirement, which facilitate compliance with the objective of Regulation YY to provide a 30-day liquidity buffer for bank holding companies.

[44] See Standard & Poor's, United States of America 'AA+/A-1+' Ratings Affirmed, June 10, 2013 ("June 10, 2013—Standard & Poor's Ratings Services today affirmed its 'AA+' long-term and 'A-1+' short-term unsolicited sovereign credit ratings on the United States of America. The outlook on the long-term rating is revised to stable from negative.").

[45] See FASB Statement of Financial Accounting Standards No. 95 (Statement of Cash Flows), n. 1 ("Consistent with common usage, cash includes not only currency on hand but demand deposits with banks or other financial institutions. Cash also includes other kinds of accounts that have the general characteristics of demand deposits in that the customer may deposit additional funds at any time and also effectively may withdraw funds at any time without prior notice or penalty.").

[46] 12 C.F.R. § 204. The regulation provides, in pertinent part: "Demand deposit means a deposit that is payable on demand, or a deposit issued with an original maturity or required notice period of less than seven days…. The term demand deposit also means deposits or accounts on which the depository institution has reserved the right to require at least seven days' written notice prior to withdrawal or transfer of any funds in the account. . . ." 12 C.F.R. § 204.2(b)(1). "Transaction account includes . . . (1) Demand deposits; (2) Deposits or accounts on which the depository institution has reserved the right to require at least seven days' written notice prior to withdrawal or transfer of any

The term "demand deposit" in Regulation D includes deposits that cannot be withdrawn by the depositor for up to seven days.[47] The term "transaction account" similarly includes deposits on which the bank has reserved the right to require at least seven days' prior written notice.[48] Thus, Regulation YY appears to contemplate that "highly liquid assets" will include deposits with significant withdrawal restrictions.[49]

In addition, Regulation YY also appears to treat as "highly liquid assets" both insured and uninsured bank deposits. Uninsured deposits appear to be included without regard to the financial condition of the issuing bank. Unlike insured deposits, uninsured deposits are not guaranteed by the FDIC. If a bank fails, the FDIC is legally obligated to pay depositors only up to the insured amount of $250,000.[50] A covered company using deposits to meet the liquidity buffer in Regulation YY would need to hold uninsured deposits in considerably larger amounts. Approximately one-third of all deposits in U.S. banks—more than $3 trillion—are uninsured.

MMFs are safer and more liquid than uninsured deposits, as historical experience has shown. Thousands of banks have failed in the past 35 years, including hundreds in the recent financial crisis.[51] Uninsured depositors in bank failures can expect to lose 50 percent or more of their investment.[52]

Federal Reserve economists have noted the safety advantages of MMFs over uninsured bank deposits:

> [B]ank deposits have safety disadvantages for large institutional investors whose cash holdings typically exceed

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funds in the account and that are subject to check, draft, negotiable order of withdrawal, share draft, or other similar item." 12 C.F.R. § 204.2(e).

[47] *Id*.

[48] *Id*.

[49] The Investment Company Act requires MMFs to pay redemption proceeds to redeeming shareholders within seven days. In this regard, MMFs are similar to banks that typically reserve the right to require seven days' notice of withdrawals on demand deposits but in practice provide same-day availability.

[50] The FDIC often pays uninsured depositors of failed banks, but only after a delay while the failed bank is liquidated and only if sufficient funds are available in the receivership estate of the failed bank.

[51] Since January 1, 2008, 463 FDIC-insured banks have failed. Source: Federal Deposit Insurance Corporation.

[52] See http://www.fdic.gov/bank/individual/failed/IndyMac.html ("When IndyMac was placed into Conservatorship in July of 2008, the FDIC calculated that the ultimate resolution of IndyMac would result in a recovery of approximately 50% of the uninsured deposits of IndyMac.").

> by orders of magnitude the caps on deposit insurance coverage; for these investors, deposits are effectively large, unsecured exposures to a bank. MMF shares—which represent claims on diversified, transparent, tightly regulated portfolios—would continue to offer important safety advantages relative to bank deposits.[53]

For this reason, among others, MMFs are used as short-term investments and cash management vehicles by institutional investors and fiduciaries who are particularly sensitive to financial risks. These investors include pension funds, employee benefit funds, charitable trusts, bank trust departments, corporate and municipal treasurers, the FDIC receivership account, and other institutional money managers acting as fiduciaries on behalf of millions of retirees, employees, taxpayers, and clients. For sound reasons, these investors prefer MMFs to uninsured bank deposits for their large cash positions.

C. The Funds are More Liquid than Some GSE Securities

The definition of "highly liquid asset" includes securities issued by Fannie Mae and Freddie Mac.[54] These government-sponsored entities were placed into conservatorship by the U.S. Treasury Department in 2008 and currently operate under the support and control of the Treasury and Federal Housing Finance Agency. These GSEs' securities are not explicitly guaranteed by the U.S. government. Similarly, securities issued by other GSEs, including the Federal Home Loan Bank System and Farm Credit System, are not explicitly guaranteed by the U.S. government.

Federated U.S. Cash Reserves and Federated Treasury Obligations Fund do not hold any GSE securities in their portfolios.

Federated Government Obligations Fund holds over 90 percent of its assets in GSE securities and repurchase agreements collateralized by such securities. The Government Obligations Fund's assets are more liquid than GSE securities that may be held as highly liquid assets under Regulation YY, however, because the Funds hold only short-term GSE securities. Regulation YY imposes no maturity limit on GSE securities held by a bank holding company in its liquidity buffer. A bank holding company may hold long-term GSE securities in

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[53] Patrick E. McCabe, Marco Cipriani, Michael Holscher, and Antoine Martin, Working Paper 2012-47, Federal Reserve Board Finance and Economics Discussion Series (July 2012) at 52.

[54] Regulation YY defines a "government sponsored enterprise" as "an entity originally established or chartered by the U.S. government to serve public purposes specified by the U.S. Congress, but whose obligations are not explicitly guaranteed by the full faith and credit of the United States." 12 C.F.R. § 252.2(x).

order to increase its yield, but with greater risk than it would incur by holding shares of the Fund.

D. The Funds Meet the Criteria for "Other" Highly Liquid Assets

Under Regulation YY, any asset may qualify as a highly liquid asset if a covered company demonstrates to the satisfaction of the Board that each of three requirements have been met. The asset must have low credit and market risk, a readily determined price, and a history of investor usage during times of stress. The Funds meet each of the three requirements.

1. Low Credit Risk

Credit risk arises from the potential that a borrower or counterparty will fail to perform on an obligation. Federated U.S. Treasury Cash Reserves has virtually no credit risk because it invests only in U.S. Treasury notes and bills, on which the risk of default is all but nonexistent. Federated Treasury Obligations Fund, which similarly invests in U.S. Treasury securities and repurchase agreements collateralized by such securities, also has virtually no credit risk for the same reason. Federated Government Obligations Fund, which invests in U.S. Treasury, U.S. government agency and GSE securities, and repurchase agreements collateralized by such securities, also has very low credit risk.

Repurchase agreements may be subject to credit risks, depending on the collateral and counterparty used. If repos are transacted with strong counterparties and secured by highly liquid assets, the credit risk is low. The Board has stated that reverse repurchase agreements may be treated as highly liquid assets.[55] Reverse repurchase agreements are simply repurchase agreements from the borrower's, as opposed to lender's, standpoint.

To limit repo counterparty risks, the Funds enter into repurchase agreements only with highly-rated dealer firms and banks—mainly primary dealers who are counterparties used by the Federal Reserve Bank of New York in its open market operations and repurchase agreements. The Funds monitor their

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[55] 79 Fed. Reg. at 17260 ("Several commenters requested clarification on how to account for reverse repo transactions, particularly those secured by highly liquid assets, in the buffer and how the tenor of the agreement would play a role in the availability of the asset in a company's highly liquid asset calculation under the proposed rule. The Board clarifies that if firms are able to rehypothecate collateral they hold that has been pledged to them to secure a loan (but have not done so), they may count that collateral as a highly liquid asset with appropriate haircuts. Appropriate haircuts and measurements of inflows and outflows would depend on the specific terms of the reverse repo transaction.").

repo counterparties as well as the amount and duration of the Funds' repo transactions with them.

To ensure the Funds have a perfected security interest in the repo collateral, a custodian for the Fund (or sub-custodian in the case of a tri-party arrangement) takes possession of the collateral. The Funds (or the sub-custodian) use an independent pricing source to value the collateral on a daily basis and assure the market value is appropriate. Any discrepancies are reconciled within the same business day. The collateral must equal at least 102 percent of the money advanced to the counterparty for all security types. Most of the Funds' repo agreements are on an overnight basis. For repo agreements with a term longer than one day, the collateral is re-priced each day, and any additional collateral required from the counterparty must be sent to the custodian or sub-custodian on a timely basis that day. The Funds have the ability to terminate any term repo agreement with seven days' notice.

In the unlikely event a counterparty goes bankrupt, the Funds are protected by a special safe harbor provision in the Bankruptcy Code that exempts repurchase agreements from the Code's automatic stay provisions and allows a debtor access to the collateral underlying its repurchase agreements.[56]

The main credit risk in a repurchase agreement is that, in the event of a counterparty default, the repo seller might be left holding the collateral and need to sell it at a "fire sale" price. The particular risk for a MMF in the event of a counterparty default is that the maturity of the collateral securities might be longer-term and, when added to the fund's portfolio, cause the fund to exceed the maturity provisions of Rule 2a-7, thereby necessitating that the fund sell off longer-term securities prior to their maturity. The risk of a "fire sale" in the case U.S. Treasury, government agency, and GSE securities is remote, however, given the depth and liquidity of the market for such securities.[57] Moreover, the "fire

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[56] 11 U.S.C. § 559 ("The exercise of a contractual right of a repo participant . . . to cause the liquidation, termination or acceleration of a repurchase agreement . . . shall not be stayed, avoided, or otherwise limited by operation of any provision of this title or by order of a court.").

[57] Among other things, the Federal Reserve Bank of New York uses the repo market as a means of implementing monetary policy actions of the Federal Open Market Committee. See http://www.newyorkfed.org/aboutthefed/fedpoint/fed04.html ("Repos are the most common form of temporary open market operation."). See also Brian Begalle Antoine Martin James McAndrews Susan McLaughlin, The Risk of Fire Sales in the Tri-Party Repo Market, Federal Reserve Bank of New York, Staff Report No. 616 May 2013 ("…the risk of fire sales of Treasuries seems remote…. A large position in government and agency securities could take time to liquidate in an orderly manner, and the potential for mark-to-market or even realized losses exists. However, several factors make that risk relatively small. Government and agency securities are generally less

sale" risk of such securities is not greater than if a bank holding company *directly* held the securities as part of its short-term liquidity buffer and was forced to liquidate the securities to meet liquidity demands.

2. Low Market Risk

Market risk involves the risk of financial loss resulting from changing market prices. The Board defines market risk as follows:

> Market risk encompasses the risk of financial loss resulting from movements in market prices. Market risk is rated based upon, but not limited to, an assessment of the following evaluation factors:
>
> - The sensitivity of the financial institution's earnings or the economic value of its capital to adverse changes in interest rates, foreign exchanges rates, commodity prices, or equity prices.
> - The ability of management to identify, measure, monitor, and control exposure to market risk given the institution's size, complexity, and risk profile.
> - The nature and complexity of interest rate risk exposure arising from nontrading positions.
> - Where appropriate, the nature and complexity of market risk exposure arising from trading and foreign operations.[58]

The primary market risk for the Funds is posed by fluctuating interest rates. Prices of U.S. Treasury and government agency securities rise and fall in response to changes in interest rates paid by similar securities. When interest rates rise, prices of such securities generally fall. Interest rate changes have a greater effect on the price of securities with longer maturities. The Funds minimize this risk by purchasing short-term securities, as required by the liquidity and maturity provisions of Rule 2a-7. MMFs also are routinely stress tested for interest rate risk.

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subject to price volatility than risk assets, in part because the former are traded in deep and liquid markets. Treasuries in particular tend to be in high demand in the event of broader market stress and are beneficiaries of a broad flight to quality. In addition, margins on government and agency collateral in the tri-party market today would be adequate, in most cases, to absorb the likely scope of mark-to-market losses, provided there is no undue pressure to liquidate the securities immediately.").

[58] Federal Reserve Board, Supervisory Policy and Guidance Topics—Market Risk Management, http://www.federalreserve.gov/bankinforeg/topics/market_risk_mgmt.htm.

The Funds are not exposed to market risk with respect to commercial paper, certificates of deposit, or foreign securities because they do not hold such assets.

Regulation YY requires that, in calculating the amount of a highly liquid asset, a covered company must discount the fair market value of the asset to reflect any credit risk and market price volatility of the asset. In the case of the Funds, a company may make this calculation using the Funds' market-value NAV, which generally does not deviate from $1.00 but is available for this purpose should the Board deem it necessary.

3. Ready Price Determination

The second prong of the Regulation YY test for "other" highly liquid assets requires that the asset be offered in such a manner that a price can be determined within one day and settled at that price within a reasonable period of time.[59]

Each Fund is operated so that it maintains a stable $1.00 net asset value and thus the price of $1.00 per share can be determined immediately and settled at that price within a reasonable time period conforming with trade custom—i.e., the same day—without the need for a secondary market. The bid and sales price of the Fund is always the same—$1.00 per share.

The assets held by the Funds trade in an active, highly liquid secondary market in which market making is supported by, among other market participants, the 22 trading counterparties of the Federal Reserve Bank of New York designated as primary dealers of U.S. government debt.[60]

[59] The language of the Regulation states that the asset must be "traded in an active secondary two-way market that has committed market makers and independent bona fide offers to buy and sell so that a price reasonably related to the last sales price or current bona fide competitive bid and offer quotations can be determined within one day and settled at that price within a reasonable time period conforming with trade custom." The price of money market funds is established and thus shares of such funds are not traded in the secondary market.

[60] As of March 26, 2014, the average daily volume of primary dealer transactions in U.S. government securities was approximately $563 billion and in U.S. government agency and GSE securities approximately $39 billion. Federal Reserve Bank of New York, Primary Dealer Transactions in U.S. Government, Federal Agency, Government Sponsored Enterprise, Mortgage-backed, and Corporate Securities, State and Municipal Government Obligations, and Asset-backed Securities by Type of Counterparty, for week ended March 26, 2014.

4. Performance Under Stress

The third prong of the test for "other" highly liquid assets requires that it be a "type of asset that investors historically have purchased in periods of financial market distress during which market liquidity has been impaired." The Funds are a type of MMF to which investors transfer assets for safety during periods of financial market distress.

For example, at the height of the financial crisis during September 2, 2008 to October 7, 2008, total assets in all government MMFs increased by $409 billion, or 44 percent.[61] Total assets in all MMFs increased by approximately $750 billion from January 2008 to January 2009 during the financial crisis.[62]

As noted earlier, the Funds also experienced substantial asset gains during the financial crisis. During the period September 2, 2008 to December 31, 2008:

> Federated U.S. Treasury Cash Reserves gained $35.7 billion or 253 percent in assets;
>
> Federated Treasury Obligations Fund gained $8.9 billion or 35.6 percent in assets; and
>
> Federated Government Obligations Fund gained $27.5 billion or 91.5 percent in assets.

During the period September 2, 2008 to October 7, 2008:

> Federated U.S. Treasury Cash Reserves increased from $14.1 billion to $36.1 billion in assets;
>
> Federated Treasury Obligations Fund increased from $25 billion to $34.5 billion in assets; and
>
> Federated Government Obligations Fund increased from $30 billion to $39.9 billion.

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[61] Securities and Exchange Commission, Division of Risk, Strategy, and Financial Innovation, Response to Questions Posed by Commissioners Aguilar, Paredes, and Gallagher, Nov. 30, 2012, at 7. Total net assets in government-only MMFs were $760 billion in 2007, $1.5 trillion in 2008, $1.1 trillion in 2009, $855 billion in 2010, $970 billion in 2011, and $929 billion in 2012. Investment Company Institute, 2013 Mutual Fund Fact Book, Table 39.

[62] Source: Investment Company Institute, Weekly Total Net Assets and Number of Money Market Mutual Funds. More than half of the increased assets came into MMFs prior to the bankruptcy of Lehman Brothers on September 15, 2008.

During the financial crisis, investors fled the stock market, which dropped precipitously and lost nearly 50 percent of its value whereas MMFs continued to pay their shareholders $1.00 per share.[63]

During the market instability associated with the U.S. government's potential default on its securities in August of 2011, government MMFs experienced increased outflows but had no difficulty meeting shareholder redemptions.[64] Shareholder levels rose shortly after Congress passed legislation increasing the debt ceiling. From July to September 2011, Federated U.S. Treasury Cash Reserves gained approximately $2.0 billion in assets (12.9 percent), Federated Treasury Obligations Fund gained $4.3 billion in assets (22.9 percent), and Federated Government Obligations Fund gained $1.4 billion in assets (4.0 percent). None of the Funds experienced a fluctuation of more than one basis point in its market-based NAV (i.e., $0.0001).

E. The Funds are More Liquid Than "Other" Highly Liquid Assets

Regulation YY contemplates that "other" assets determined by the Board to be highly liquid and eligible to be included in a covered company's liquidity buffer may include sovereign debt securities, investment grade corporate debt securities, and debt securities issued by companies included in the S&P 500 Index.[65] Many of such assets have not been traditionally thought of as "highly liquid" in the financial marketplace.

In particular, equity securities of companies that make up the S&P 500 Index have not been considered as highly liquid. The companies in the Index

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[63] One prime MMF that invested in commercial paper failed to pay $1.00 but its shareholders ultimately received $.99 per share upon the fund's liquidation. No other major MMF ever has "broken the dollar." A small MMF broke the dollar in 1994 and paid its shareholders $.96 per share.

[64] MMF shareholders withdrew approximately $54 billion from government MMFs in July of 2011. ICI Research Perspective, Vol. 19, No. 1, Jan. 2013. In order to avoid issues created by a Treasury default, some fund shareholders shifted cash to demand deposits at banks that had unlimited federal insurance at the time, which since has expired.

[65] The Board's Federal Register notice states that "other" highly liquid assets generally would include assets that qualify as "high-quality liquid assets" under the pending proposed Basel III Liquidity Coverage Ratio ("LCR"), assuming the other requirements of the regulation are met. 79 Fed. Reg. at 17259. Those assets include equities included in the S&P 500 index or comparable indices, investment grade corporate bonds, and sovereign debt securities that meet certain requirements. See Liquidity Coverage Ratio: Liquidity Risk Measurement, Standards, and Monitoring, 78 Fed. Reg. 71818 (Nov. 29, 2013).

engage in a wide range of commercial activities, including the manufacturing or selling of automobiles, refrigerators, pharmaceuticals, chemicals, homes, office buildings, computer equipment, apparel, shoes, shampoo, personal accessories, energy, food, office supplies, paint, peanut butter, jelly, tobacco, candy, jewelry, cartoons, and travel services. The Index also includes a number of banks, securities broker-dealers, and other financial service firms whose equity securities are not considered highly liquid.

None of equity securities in the S&P 500 Index are permissible investments for a money market fund, or a national bank. None of such securities are considered as highly liquid for any of the regulatory purposes discussed earlier in this memorandum. The degree of liquidity provided by such investments is substantially lower than that afforded by either a prime money market fund that invests only in short-term, high-quality debt securities, or a government money market fund—such as the Funds—that invests only in U.S. Treasury, U.S. government agency, and GSE securities and repurchase agreements collateralized by such securities.

Regulation YY would allow such equity securities to be considered highly liquid assets even if their market value drops by as much as 40 percent during a 30-day period of stress. During the financial crisis in 2008-2009, the S&P 500 Index fell by more than 50 percent.[66] In contrast, no government MMF failed to pay its investors less than the full value of $1.00 per share.[67] Said another way, investors in S&P 500 Index companies lost more than 50 percent of their investments, whereas investors in government MMFs lost *none* of theirs. As noted previously, government MMFs retained their liquidity and gained substantial assets during the crisis.

It seems unlikely that the Board intends to use the 2008-2009 financial crisis as the appropriate 30-day period for determining the liquidity of S&P 500 Index equities, since few if any of them would qualify. In any event, the facts show that money market funds are far more liquid than the types of "other" assets contemplated to be treated as highly liquid under Regulation YY.

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[66] See Gerald P. Dwyer, Stock Prices in the Financial Crisis, Federal Reserve Bank of Atlanta, September 2009, http://www.frbatlanta.org/cenfis/pubscf/stock_prices_infinancial_crisis.cfm.

[67] As noted, one prime MMF broke a dollar but paid its shareholders $0.99 per share upon liquidation.

VI. CONCLUSION

This memorandum demonstrates how Federated U.S. Treasury Cash Reserves, Federated Treasury Obligations Fund, and Federated Government Obligations Fund meet the definition of highly liquid assets for purposes of the Regulation YY liquidity buffer. Accordingly, we respectfully request the Board of Governors to issue a determination that the Funds are highly liquid and eligible to be included in a covered company's liquidity buffer for purposes of Regulation YY, assuming the company meets the other requirements in the regulation.

APPENDIX--REGULATION OF MMFS

Money market funds are highly regulated under the Investment Company Act of 1940 and Rule 2a-7 of the Securities and Exchange Commission thereunder.[68] The Rule imposes stringent credit quality, liquidity, diversification, transparency, and other requirements on MMFs. These requirements are summarized below.

A. Credit Quality

Under Rule 2a-7, a MMF may invest in only high quality, short-term instruments rated in the top two categories by a nationally recognized ratings organization and that present minimal credit risk. Each MMF must perform an independent credit analysis of every security it purchases. MMFs generally are not permitted to use leverage in their investment portfolios.

B. Liquidity

Under Rule 2a-7, MMFs are required to maintain a weighted average portfolio maturity of 60 days or less and a weighted average portfolio life of 120 days or less. Each MMF must be able to liquidate 10 percent of its portfolio assets within one day and 30 percent within five business days. MMFs may hold no more than five percent of their assets in illiquid securities (i.e., that cannot be liquidated at approximately the value ascribed to them by the fund in seven days).

In addition, each MMF is required to hold securities that are sufficiently liquid to meet reasonably foreseeable shareholder redemptions (the general liquidity requirement), which may require a fund to maintain greater liquidity than the daily or weekly requirements.

C. Diversification

Under Rule 2a-7, a MMF generally may invest no more than five percent of its assets in securities of any one issuer, with an exception for U.S. government securities and repurchase agreements collateralized by such securities.

D. Market Valuation

MMFs are required to calculate the market value of their assets on a regular basis. Although Rule 2a-7 permits MMFs to value their portfolio securities at acquisition cost as adjusted for amortization of premium or accretion of discount—the so-called amortized cost method of accounting—MMFs

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[68] 17 C.F.R. § 270.2a-7.

nevertheless also are required to value their assets based on market values—so-called "shadow pricing." In this regard, MMFs must adopt written procedures requiring the periodic calculation of "the extent of deviation, if any, of the current net asset value per share calculated using available market quotations . . . from the money market fund's amortized cost price per share." If any deviation from the fund's amortized cost price per share may result in material dilution or other unfair results to investors, the fund must take such action as is reasonably practicable to eliminate or reduce the dilution or unfair results, including by liquidating.

E. Transparency

MMFs are required to make extensive disclosures about their operations, activities, investments, risks, service providers, fees, and other matters in prospectuses and other information filed with the SEC and made available to investors. They also are required to disclose detailed information about each investment in their portfolios, including the name of the issuer, category of investment, CUSIP number, principal amount, maturity date, final legal maturity date, coupon or yield, and amortized cost value.

F. Stress Testing

Each MMF is required to adopt procedures providing for the periodic testing of the fund's ability to maintain a stable net asset value per share based on certain hypothetical events, including: an increase in short-term interest rates, an increase in shareholder redemptions, a downgrade of or default on portfolio securities, and a widening or narrowing of spreads between yields on an appropriate benchmark selected by the fund for overnight interest rates and commercial paper and other types of securities held by the fund. The SEC expects a MMF to conduct weekly stress tests if its net asset value decreases to less than $0.9975.

G. Shareholder Equality

MMFs are required to treat all shareholders of the same class of fund shares equally. They are prohibited from issuing senior securities or otherwise treating shareholders of the same class disparately. Each share of a MMF must have equal voting rights with all other shares in the fund.

H. Governance

Each MMF is governed by a board of trustees or directors, 40 percent of whom must be independent from fund management. The board of trustees oversees the operations and management of the fund and protects fund shareholders.

I. Transactions With Affiliates

MMFs may not make any loans to or purchase any securities issued by or from an affiliated person, absent an exemption by the SEC. The Investment Company Act restricts a wide range of transactions and arrangements involving funds and their affiliates. The Act's provisions protect MMFs and other registered investment companies from self-dealing and overreaching by affiliated persons. Among other things, the Act prohibits any affiliated person of a MMF from knowingly purchasing securities or other property from the fund and prohibits a MMF from engaging in any transaction in which an affiliate is a joint participant unless allowed by SEC rules.

J. Other Limitations

MMFs do not have the ability to create off-balance sheet liabilities. All of their assets are carried on-balance sheet. MMFs are not permitted to own operating companies or other subsidiaries.

K. Orderly Liquidation and Loss Minimization

MMFs have the capacity to self-liquidate and return each investor's pro rata share of the fund's assets in a relatively simple process. A fund's board of directors may decide to liquidate the fund for a variety of reasons. For example, a number of funds in 2012 liquidated or merged with other funds after their investment advisers decided to exit the MMF business.[69] Several MMFs underwent orderly liquidations during the financial crisis.[70] Investors in the liquidated funds received $1.00 per share.

[69] See Crane Data reports dated Dec. 18, Nov. 13, Oct. 25, and Aug.21, 2012, reporting MMF liquidations. www.cranedata.com.

[70] For example, one MMF announced that its board of trustees on February 20, 2009, had approved the liquidation of the fund, which would be closed to new investors and additional purchases by existing investors as of May 1, 2009, and that the fund would be liquidated as of the close of business on or about May 15, 2009. Investors were permitted to either exchange into other funds of the sponsor without sales charges or to redeem at any time prior to liquidation. Investors who did not exchange or redeem their shares were told their shares would be liquidated and they would be paid liquidation proceeds. See Calamos Government Money Market Fund 2009 prospectus, p. 9. See also New York Times, Professional Money Fund Is Closed by Putnam, by Diana B. Henriques, Sept. 18, 2008. The Putnam fund suspended redemptions rather than sell assets into the marketplace and risk losses for non-redeeming investors. Federated Investors, Inc. made an in-kind purchase of the fund's assets, the fund's shareholders received an equivalent amount of shares of a Federated MMF, and the fund was liquidated in a prompt and orderly manner with no loss to investors.

Rule 2a-7 permits a MMF's board of directors to suspend redemptions and liquidate if it appears the fund may break the buck or if a material dilution or other unfair results to investors may follow from a deviation between the fund's amortized cost price and its market-based NAV.[71] If a MMF does break a dollar—which has occurred only twice ever—the fund no longer is permitted to operate with a $1.00 NAV. In that event, the fund will be closed immediately and not generate further losses.[72] The fund's shareholders do not lose their investment but are entitled to a pro rata share of the fund's assets upon liquidation.

By requiring a MMF effectively to cease operating if its market-based NAV falls half a penny below a dollar, the SEC's rules ensure that investor losses are minimal if the fund breaks the buck. A vivid illustration of the loss-limiting effect of the rules is the return of more than 99 cents on the dollar to investors of the Reserve Primary Fund (not a government-only MMF) after that fund broke the buck in 2008 and was liquidated.[73]

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[71] See SEC Rule 22e-3, 17 C.F.R. § 270.22e-3. The fund's board must notify the SEC of its decision to liquidate the fund.

[72] A MMF that "breaks the buck" theoretically could operate with a floating NAV but would not be competitive as a practical matter. It thus is expected that any MMF that breaks a dollar will close.

[73] A fund may be liquidated in a relatively short period of time because of the short maturity of its portfolio. The Reserve Primary Fund was liquidated in a court-supervised process that took approximately one year due to allegations of fraud by the SEC, but shareholders received most of their assets in phases early in the process. See http://www.primary-yieldplus-inliquidation.com/pdf/PrimaryDistribution_71510.pdf.