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August 6, 2007

Nancy J. Morris
Secretary
U. S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

Re: File Number S7-08-07

Dear Ms. Morris:

On behalf of our client, Federated Investors, Inc. (“Federated”) we wish to supplement our comments to the Securities and Exchange Commission (the “Commission” or the “SEC”) on Securities Exchange Act Release No. 55431.¹ Although we have filed an extensive comment letter on the Release,² we wish to address some comments that the Securities Investor Protection Corporation (“SIPC”) made in its letter.³

At page 2 of its letter, SIPC states:

The Commission proposes to broaden the definition of “qualified securities” to include certain money market funds. Notwithstanding the asserted convenience and reliability of

¹ March 9, 2007; 72 FR 12899 (March 19, 2007) (the “Release”).

² Letter from Stuart J. Kaswell and David J. Harris, Dechert, LLP, May 1, 2007 (the “Federated Letter”).

³ Letter from Josephine Wang, General Counsel, May 17, 2007.

such investments, SIPC endorses the Proposal with reservation for at least two reasons. One, the Proposal introduces an intermediary (namely, the holding company or money market fund) at which problems might arise. And two, a number of SIPA liquidations have involved the mishandling of money market or mutual fund shares or the confirmation of purchases of nonexistent "money market funds." Experience suggests that a money market fund that "invests in nothing but qualified securities" may be more easy to falsify than the qualified securities themselves.

Federated respectfully disagrees with these comments for several reasons. To comply with Rule 15c3-3(e), a broker-dealer must establish a special reserve account that satisfies the requirements of the rule. Under current law, the broker-dealer must either deposit cash or qualified securities⁴ into the account. We discuss both alternatives in turn.

A. If the broker-dealer deposits cash, the funds become subject to the bank's balance sheet. There are at least two consequences to that fact:

- The assets into which a bank is likely to invest the funds in the special reserve account may not be of as high quality as the portfolio securities of a AAA-rated money market mutual fund. As noted in the Federated Letter, 100% of the assets of a AAA-rated money market mutual fund must be invested in securities that are rated A-1 or better. By comparison, only about 30% of the assets of commercial banks are invested in assets of that quality.⁵
- Moreover, there is no banking law requirement to segregate the assets in which the special reserve accounts invests. Again, the cash in the special reserve account becomes part of the bank's balance sheet. By comparison, Section 17(f)(1) of the Investment Company Act of 1940 requires, among other things, that "every registered management Company place and maintain its securities and similar investments in the custody of" a bank or certain other specified financial institutions.⁶

⁴ Rule 15c3-3(a)(6) defines "qualified security" as a security issued by the United States or a security in respect of which the principal and interest are guaranteed by the United States.

⁵ The Federated Letter at 7 and Attachment II discuss the risks inherent in bank deposits compared with AAA-rated money market funds in greater detail.

⁶ See also Rules 17f-1 through 7 (17 CFR §270.17f-1 through 7) and Frankel, 2 The Regulation of Money Managers (2d. ed.) at §17.03

Accordingly, it is not accurate to say that no intermediary is involved when the broker-dealer deposits cash in a bank; indeed there is an intermediary, *i.e.*, the bank. The broker-dealer's funds are subject to claims on that intermediary's balance sheet. If SIPC meant to suggest that adding a AAA-rated money market mutual fund adds another intermediary in the process, that intermediary will invest the proceeds exclusively in high quality assets and segregate them, unlike a bank. As a result, the cash in a broker-dealer's special reserve account is at least as safe, and probably safer, when invested in a AAA-rated money market mutual fund, than when held on a bank's balance sheet. We therefore see no disadvantage to adding another intermediary and, indeed, believe that there are advantages to adding another intermediary when it is a AAA-rated money market mutual fund.

B. If the broker-dealer deposits qualified securities, there are certain complexities involved in such transactions:

- There are operational risks involved in the purchase and sale of U.S. Treasury securities. As the Commission notes in the Release, there are "operational aspects of holding and managing U.S. Treasury securities...."⁷ In Federated's view, the operational risks of purchasing and selling individual U.S. Treasury securities are considerable and it is our experience that even the largest broker-dealers would prefer to use AAA-rated money market funds to maintain the special reserve account.
- Broker-dealers that deposit qualified securities in the special reserve account do not use exclusively physical certificates, again involving the use of one or more intermediary banks in the process.⁸

⁷ Release at 12865.

⁸ The SEC's Division of Market Regulation has issued guidelines for handling qualified securities, which include in part:

Physical Certificates: The bank actually holding the certificates must acknowledge to the broker-dealer in writing that the certificates are identified on the bank's books as being held free of lien in a special account for the exclusive benefit of customers of the broker-dealer.

Uncertificated Securities: The bank having the direct access to the Federal Reserve bank book entry system must acknowledge in writing to the broker-dealer that the securities are held free of any lien in a special reserve account for the exclusive benefit of customers of the broker-dealer.

We also do not agree with the suggestion that it is easier to falsify an account with money market mutual funds than with other qualified securities or cash. It is our belief that it is no more or less difficult for a fraudster to create bogus statements indicating that the account contains a money market fund, than it is to create bogus statements indicating that the account holds cash or U.S. Treasury securities. A determined crook will have no compunction about lying in either case, and we believe false statements showing one type of asset or another would be no more or less identifiable in either event. Accordingly, we see no basis for denying legitimate broker-dealers the benefits of using AAA-rated money market funds for the special reserve account.

To date, SIPC is the only commentator raising objections to the Commission's proposed expansion of the definition of "qualified securities" to include Treasury-only money market mutual funds.⁹ Indeed, every other commentator addressing the issue has suggested that the

Reverse Repurchase Agreement Securities: Possession or control must be established as in the appropriate paragraph above.

http://www.nasd.com/web/idcplg?IdcService=SS_GET_PAGE&siteId=5&siteRelativeUrl=%2FRulesRegulation%2FPublicationsGuidance%2FInterpretationsofFinancialOperationalRules%2FCustomerProtectionRule_SECRule15c3%2D3%2FNASDW_016818&ssUrlPrefix=/&PrinterFriendly=1

⁹ The Commission proposes that to amend Rule 15c3-3(a)(6) to provide, in part, that:

The term *qualified security* shall mean:

- (i) A security issued by the United States or guaranteed by the United States with respect to principal or interest; and
- (ii) A redeemable security of an unaffiliated investment company registered under the Investment Company Act of 1940 and described in § 270.2a-7 of this chapter that:
 - (A) Has assets consisting solely of cash and securities issued by the United States or guaranteed by the United States with respect to principal and interest;

Release, at 12894. We refer to such money market mutual funds as "Treasury-only" money market mutual funds.

Commission should broaden the definition further to include more varieties of money market mutual funds.

We have the highest regard for the role that SIPC plays in the protection of investors, and have the greatest respect for SIPC's staff. Nonetheless, we respectfully disagree with SIPC's comments regarding the special reserve account under Rule 15c3-3.

Please contact us if you have any questions.

Sincerely yours,

/s/

Stuart J. Kaswell
Partner

/s/

David J. Harris
Partner

c: The Honorable Christopher Cox, Chairman
The Honorable Paul S. Atkins, Commissioner
The Honorable Roel C. Campos, Commissioner
The Honorable Annette L. Nazareth, Commissioner
The Honorable Kathleen L. Casey, Commissioner
Erik R. Sirri, Ph.D., Director, Division of Market Regulation
Andrew Donohue, Director, Division of Investment Management
Robert L.D. Colby, Deputy Director, Division of Market Regulation
Michael A Macchiaroli, Associate Director, Division of Market Regulation
Robert E. Plaze, Associate Director, Division of Investment Management
Thomas McGowan, Assistant Director, Division of Market Regulation

The Honorable Gregory W. Meeks, U.S. House of Representatives
The Honorable Patrick J. Tiberi, U.S. House of Representatives

Josephine Wang, General Counsel, SIPC

Eugene F. Maloney, Executive Vice President, Federated Investors Management Company, Inc., Vice President and Corporate Counsel of Federated Investors, Inc. and member of the Executive Committee.