

PICKARD AND DJINIS LLP

ATTORNEYS AT LAW

1990 M STREET, N.W., SUITE 660

WASHINGTON, D.C. 20036

WWW.PICKDJIN.COM

TELEPHONE
(202) 223-4418

FACSIMILE
(202) 331-3813

June 1, 2012

VIA email (rule-comments@sec.gov)

Ms. Elizabeth M. Murphy

Secretary

Securities and Exchange Commission

100 F Street, N.E.

Washington, D.C. 20549-1090

Re: File No. S7-08-07; RIN 3235-AJ85 – Proposed Rulemaking Regarding
Amendments to Financial Responsibility Rules for Broker-Dealers

Dear Ms. Murphy:

This letter presents comments on behalf of Federated Investors, Inc.¹ (“Federated”) on the Commission’s reconsideration of the proposed amendments to the customer protection rule (Rule 15c3-3) initially proposed by the Commission in “Amendments to Financial Responsibility Rules for Broker-Dealers, Proposed Rule,” 72 Fed. Reg. 12861 (Mar. 19, 2007)(the “2007 Rule Proposal”).

In the 2007 Rule Proposal, the SEC proposed, among others, to expand Rule 15c3-3(a)(6) to include money market funds that only invest in securities meeting the definition of “qualified securities” in Rule 15c3-3.² As Federated stated then – and which continues to be true today –, there is a demand in the broker-dealer industry for greater options to place undeployed customer

¹ Federated and its subsidiaries, as of March 31, 2012, manage approximately 134 mutual funds with over \$363 billion in assets under management. Of those, 48 are money market funds containing \$245 billion in assets.

² Under the 2007 Rule Proposal, the term “qualified security” would be amended to include, “A redeemable security of an unaffiliated investment company registered under the Investment Company Act of 1940 and described in Sec. 270.217 of this chapter that: (A) Has assets consisting of solely of cash and securities issued by the United States or guaranteed by the United States with respect to principal and interest; (B) Agrees to redeem fund shares in cash no later than the business day following a redemption request by a shareholder; and (C) Has net assets (assets net of liabilities) equal to at least 10 times the value of the fund shares held by the broker-dealer in the customer reserve account required under paragraph (e) of this section. See 2007 Proposed Rule, 72 Fed. Reg. 12861, 12894.

funds. Broker-dealers, who are customers of Federated, maintain significant funds in their Special Reserve Accounts to meet their Rule 15c3-3 deposit requirements.³ It is estimated that aggregate requirements for deposits in Rule 15c3-3 segregated accounts at times have exceed 180 billion dollars. The proposed amendment, if adopted, will provide a much needed additional option; improve broker-dealers' operational flexibility in meeting their obligations under Rule 15c3-3; avoid the burdens of actively managing a portfolio of U.S. Treasuries; and will allow broker-dealers to obtain more competitive yields on such assets while, at the same time, not compromise the Rule 15c3-3's Congressional purpose of safeguarding customers' deposits or credit balances.⁴

Indeed, U.S. government money market funds are closely related to U.S. Treasury securities and cash. Investing customer funds segregated in a Rule 15c3-3 account in U.S. government money market funds, U.S. Treasuries, or interest-bearing checking accounts serves the same purpose – to protect the value of a customer's funds with little risk to the customer due to the non-speculative, liquid nature of these types of holdings. The financial markets as well as the Commission recognize money market funds as cash items. The Financial Accounting Standards Board (“FASB”), the highest authority in establishing generally accepted accounting

³ As noted in the rule proposal, Federated was an initial proponent for amending Rule 15c3-3 to include money market funds as meeting the customer reserve deposit requirements under Rule 15c3-3.

⁴ For additional comment concerning broker-dealer demand and the operational utility of U.S. government money market funds, see Comment from Rep. Gregory W. Meek, U.S. House of Representatives (Oct. 14, 2011) <http://www.sec.gov/comments/s7-08-07/s70807-81.pdf>; Comment from Lee A. Pickard (Nov. 10, 2008) <http://www.sec.gov/comments/s7-08-07/s70807-76.pdf>; Comment from Lee A. Pickard (Nov. 25, 2008) <http://www.sec.gov/comments/s7-08-07/s70807-77>; Comment from Lee A. Pickard, Pickard and Djinis LLP, on behalf of Federated Investors, Inc. (Dec. 18, 2008) <http://www.sec.gov/comments/s7-08-07/s70807-78.pdf>.

principles for public and private companies, identifies money market funds as cash equivalents,⁵ and the Commission has acknowledged that “money market fund shares generally are equivalent to cash items.”⁶ Accordingly, U.S. government money market funds should be included under the definition of “qualified securities.”⁷

Safety of U.S. Government Money Market Funds

Since the 2007 Rule Proposal release, the financial industry has experienced the 2008 financial crisis, bringing into question the credit and liquidity risks attendant to a number of business practices. Here, however, given the very restrictive composition of the portfolio which would be allowed for a U.S. government money market fund (i.e., only securities issued or guaranteed by the United States Government⁸ or cash), the issue of credit worthiness and liquidity is satisfactorily addressed. The portfolio of a U.S. government money market fund would not be subject to default. Nor would a U.S. government money market fund portfolio be without ready buyers or sellers if the need arose, as the U.S. government securities market is extremely liquid.

The safety record of U.S. government money market funds further supports the acceptability of this financial instrument for Rule 15c3-3 deposit requirements. There have been

⁵ See FASB ASC 305-10-20.

⁶ See *Willkie Farr & Gallagher*, SEC No Action Letter, 2000 SEC No-Act. LEXIS 916 (Oct. 23, 2000), noting that the SEC staff would not recommend enforcement action if an issuer, in calculating the amount of its total assets and investment securities for purposes of the “40 percent test” in Section 3(a)(1)(C) of the Investment Company Act of 1940, does not include its ownership interest in money market funds.

⁷ The Commission is also reconsidering an amendment that would reduce the current 2% “haircut” broker-dealers apply under Rule 15c3- 1 for money market funds when computing net capital. Federated believes that the haircuts on money market funds should be reduced. See Federated’s Submission to Honorable Troy A. Paredes Commissioner U.S. Securities and Exchange Commission, August 7, 2008, <http://www.sec.gov/comments/s7-08-07/s70807-71.pdf>.

⁸ Federated recommends that the Commission confirm that U.S. government money market fund portfolios may also include repurchase agreements, which are currently used by such funds.

no defaults in the type of U.S. government money market fund proposed in the 2007 Rule Proposal. Indeed, during the most volatile period of the credit crisis (September 2, 2008 through October 28, 2008), institutional U.S. government money market assets grew \$403 billion.

**CFTC Recently Designated U.S. Government Money Market Funds
As Permitted Investments for Customer Segregated Funds**

In further support of the use of U.S. government money market funds as an appropriate investment vehicle for customer segregated funds, we note that since the 2007 Rule Proposal release and the 2008 financial crisis, the Commodity Futures Trading Commission has adopted amendments to CFTC Rules 1.25 and 30.7 decisively affirming the use of U.S. government money market mutual funds as a permitted investment for customer funds held by Futures Commission Merchants under the CFTC's customer segregation rules.⁹ In determining to permit with virtually no limits the use of U.S. government money market funds,¹⁰ the CFTC analyzed the safety provided by enhanced SEC Rule 2a-7 and the equivalency of a U.S. government money market fund to a self-managed U.S. Treasury portfolio, as well as the operational and administrative efficiencies of U.S. government money market mutual funds. The Commission's fellow agency concluded that the permissible use of U.S. government money market funds for customer segregated funds is consistent with the prudential standards of preserving principal and maintain liquidity. The CFTC's findings are particularly relevant here as the SEC and the CFTC each have well-established programs for the segregation of customer funds held by a broker-dealer or FCM, and both permit the broker-dealer or FCM to place customer funds into specific

⁹ Investment of Customer Funds and Funds Held in an Account for Foreign Futures and Foreign Options Transactions, 76 Fed. Reg. 78776 (Dec. 19, 2011).

¹⁰ The CFTC permits an FCM to invest all of its customer segregated funds in Treasury-only money market funds, subject to the limitation on investments in small Treasury-only money market funds. The CFTC also permits an FCM to invest up to 50% of its customer segregated funds in any other money market fund. See Regulation 1.25.

investment options. These regimes are fundamentally the same. SEC Rule 15c3-3 requires broker-dealers to account for all customer funds held by the broker-dealer and permits customer funds to be invested in securities which enable their prompt return in the event of insolvency. Similarly, CFTC Regulation 1.20 requires FCMs to treat customer funds separately, permitting customer funds to be invested in securities which preserve principal and maintain liquidity. Attach hereto is a letter to Mr. Robert W. Cook, Director of the Division of Trading and Markets, of January 5, 2012 which highlights the CFTC's approval process for the use of U.S. government money market funds for customer segregated funds and recommends that the Commission similarly permit such use.

Conclusion

U.S. government money market funds did not exist in 1972 when the Commission adopted Rule 15c3-3 and permitted broker-dealers to deposit only cash or Treasury securities in the Reserve Account. The addition of U.S. government money market funds provides an appropriate alternative for the investment of Rule 15c3-3 customer funds and would facilitate the placement of this large pool of customer cash among a greater number of financial institutions. Federated strongly endorses the Commission's 2007 Rule Proposal to amend Rule 15c3-3(a)(6) to include U.S. government money market funds.

Ms. Elizabeth M. Murphy

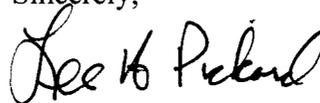
June 1, 2012

Page 6

* * * * *

Federated Investors, Inc. thanks you for this opportunity to provide updated comments on the Commission's proposed rulemaking.

Sincerely,

A handwritten signature in black ink that reads "Lee A. Pickard". The signature is written in a cursive style with a large initial "L".

Lee A. Pickard

cc: Mr. Eugene F. Maloney, Executive Vice President, Federated Investors, Inc.

PICKARD AND DJINIS LLP

ATTORNEYS AT LAW

1990 M STREET, N.W., SUITE 660

WASHINGTON, D.C. 20036

WWW.PICKDJIN.COM

TELEPHONE
(202) 223-4418

FACSIMILE
(202) 331-3813

January 5, 2012

VIA E-MAIL AND COURIER

Mr. Robert W. Cook, Director
Division of Trading and Markets
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-6628

Re: The CFTC approves the use of U.S. government money market mutual funds as a permitted investment for customer segregated funds. We recommend the SEC do the same.

Dear Mr. Cook:

On behalf of Federated Investors, Inc., we submit this letter to highlight the salient factors which the Commodity Futures Trading Commission analyzed in its recent final rule release, Investment of Customer Funds and Funds Held in an Account for Foreign Futures and Foreign Options Transactions, 76 Fed. Reg. 78776 (Dec. 19, 2011) to conclude that U.S. government money market mutual funds are an important and appropriate investment vehicle for customer segregated funds. For some time now, Federated Investors and other representatives of the securities industry have implored the SEC to take essentially identical action with respect to its segregation requirements for customer funds held by broker-dealers.

On December 19, 2011 the Commodity Futures Trading Commission adopted amendments to CFTC Rules 1.25 and 30.7 decisively affirming the use of money market mutual funds and, in particular, placing virtually no limit on the use of U.S. government money market mutual funds, as a permitted investment for customer funds held by Futures Commission Merchants ("FCMs") under the CFTC's customer segregation rules. The CFTC final rule release

succinctly analyzes the reasons for the CFTC determination to permit FCMs to invest customer funds in money market mutual funds. The important factors relied upon by the CFTC in its review of the role of U.S. government money market mutual funds in the customer fund segregation process included the safety provided by enhanced SEC Rule 2a-7, the operational and administrative efficiency of U.S. government money market funds, as well as their market equivalency to U.S. Treasury portfolios.

As you know, the SEC and the CFTC each have well-established programs for the segregation of customer funds held by a broker-dealer or FCM, and both permit the broker-dealer or FCM to place customer funds into specific investment options. These regimes are fundamentally the same. SEC Rule 15c3-3 requires broker-dealers to account for all customer funds held by the broker-dealer and permits customer funds to be invested in securities which enable their prompt return in the event of insolvency. Similarly, CFTC Regulation 1.20 requires FCMs to treat customer funds separately, permitting customer funds to be invested in securities which preserve principal and maintain liquidity.

As the SEC is currently reviewing¹ the same issues addressed by the CFTC with respect to the inclusion of U.S. government money market mutual funds as a “qualified security” for purposes of customer funds held by broker-dealers, we believe the CFTC rule release’s discussion and analysis supporting the CFTC’s determination to permit FCMs to investment customer funds into U.S. government money market funds is vitally important to the SEC’s analysis. The CFTC has determined to permit FCMs to place customer funds into U.S. government money market mutual funds without limit. Having the benefit of the CFTC’s

¹ Counsel for Federated was advised in its November 28, 2011 meeting with Deputy Director John Ramsey and Deputy Associate Director Tom McGowan of the Division of Trading and Markets that the Division is currently, actively working on revisions of certain financial responsibility rules pertaining to broker-dealers.

analysis, as well as information gathered by the CFTC from several public comment periods, the SEC should, for all the reasons noted therein, follow its fellow agency and permit broker-dealers to place customer funds into U.S government money market mutual funds.

The CFTC's amended Regulation 1.25 permits customer funds to be invested in U.S. government money market mutual funds.

As noted in the CFTC rule release, the salient aspects of the CFTC's amended Regulation 1.25 to permit customer funds to be invested in money market mutual funds are as follows:

- Investments in money market mutual funds comprising only U.S. government securities are not subject to a concentration limit, (unless such investments are in U.S. government money market funds which have less than \$1 billion in assets and/or which have a management company which has less than \$25 billion assets under management, in which case the investment may not exceed 10 percent of the total assets held in segregation by FCMs).
- Investments in all other money market mutual funds, i.e., non-U.S. government money market mutual funds, may not exceed 50 percent of the total assets held in segregation by the FCMs (with a limitation for investments in smaller money market mutual funds).²

The CFTC acknowledges that an FCM may invest all of its customer funds in money market mutual funds, by, as examples, investing entirely in large Treasury-only money market mutual funds or by investing 50 percent of its customer funds in large prime money market mutual funds (spread out among five individual funds and two fund families) and 50 percent in a large Treasury-only money market mutual fund.

The CFTC's decision to permit the unlimited use of U.S. government money market funds for customer fund segregation purposes was reached only after significant public debate and careful deliberation by the CFTC.

² Interests in any single family of non-U.S. government money market mutual funds may not exceed 25 percent of total assets held in segregation by the FCMs; and interests in any individual non-U.S. government money market mutual fund may not exceed 10 percent of total assets held in segregation by the FCMs.

Under CFTC rules, customer segregated funds must be invested 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. Toward these ends, Regulation 1.25 establishes a general prudential standard by requiring that all permitted investment be “consistent with the objectives of preserving principal and maintaining liquidity.”

In 2007, the CFTC conducted a review of the nature and extent of investment of Regulation 1.25 funds by FCMs and to assess whether any changes to the CFTC’s permitted investments would be appropriate. All registered FCMs carrying customer accounts provided responses to a series of questions.³ The CFTC then follow-up with an extensive public comment process where investors and other interests parties provided additional information and insight on the proposed use of money market funds.

In May 2009, after the September 2008 market events, the CFTC issued an advance notice of proposed rulemaking to solicit public comment concerning the CFTC’s permitted use of money market mutual funds. The brokerage and money fund industry submitted responses discussing the usefulness of money market funds and the money market funds’ continued compatibility with the CFTC’s prudential standard of “preserving principal and maintaining liquidity.” Further, in October 2010, the CFTC issued a notice of proposed rulemaking seeking comment from industry participants on the scope of permitted investments. The CFTC received 32 comment letters, each favorable to the use of money market funds.

³ During this time period, the SEC proposed amendments to the financial responsibility rules for broker-dealers. As part of these amendments, the SEC considered and proposed expanding the definition of “qualified security” to permit the use of U.S. government money market funds. At that time, the SEC asserted that “expanding the definition to include money market funds that only invest in securities meeting the definition of ‘qualified security’ in Rule 15c3-3 would be appropriate.” See Amendments to Financial Responsibility Rules for Broker-Dealers, Proposed Rule, 72 Fed. Reg. 12862, 12865 (Mar. 19, 2007).

The CFTC's approval of money market funds as a permitted investment for customer segregation reflects that agency's conclusion that such investments are "consistent with the obligations of preserving principal and maintaining liquidity."

In determining to permit unlimited use of U.S. government money market funds, the CFTC analyzed the safety provided by SEC Rule 2a-7, the equivalency to U.S. Treasury portfolios, the Reserve Fund events of September 2008, as well as the operational and administrative efficiency of U.S. government money market mutual funds.

To determine whether U.S. government money market mutual funds are consistent with the prudential standard of preserving principal and maintaining liquidity of customer funds, the CFTC considered and analyzed the following factors:

- **The CFTC determined that there is enhanced safety of money market funds under amended SEC Rule 2a-7.**

The CFTC determined that the heightened prudential standards recently imposed by the SEC make money market mutual funds an attractive investment option for customer segregated funds. This was consistent with the comments submitted by industry participants and interested parties that asserted that money market funds are safe and liquid relative to other permitted investments. The Rule 2a-7 reforms increased the safety of money market mutual funds by further constraining the maturity, enhancing the credit quality of their portfolios and safeguarding the liquidity of money funds by requiring investment of a substantial portion of the portfolio in the most liquid or shortest-term securities. The Rule 2a-7 amendments also increased oversight of money funds' financial and operational conditions, both internally by their directors and externally by the SEC.

Consistent with these views, the CFTC clearly stated that "the credit quality, maturity limitations and liquidity required by the SEC make prime money market mutual funds acceptable investments" for customer segregated funds. (p.49, fn 152)

- **The CFTC determined that the use of money market funds alleviates the ongoing burdens of managing customer funds.**

The CFTC found that permitting FCMs to invest customer funds in money market funds allows an FCM to delegate the management of its customer funds portfolio. As compared to the alternative of investing in individual securities, money market mutual funds provide administrative and operational advantages, in that an FCM or broker-dealer has the option of being able to avoid the burdens of actively managing a portfolio of, for example, U.S. Treasuries. The assets held by a U.S. government money market mutual fund would be the same as that the broker-dealer would otherwise hold directly in its segregated customer account.

Under the CFTC amended regulations, FCMs may delegate the entire burden of actively managing their customer fund portfolios to money market mutual fund managers.

- **The CFTC determined that U.S. government money market funds are the equivalent of a self-managed Treasury portfolio.**

The CFTC agreed with public comments in allowing investment of customer funds without asset- or issuer-based limitations for Treasury-only money market mutual funds due, in part, to the fact that Regulation 1.25 allows direct investments entirely in Treasuries. The CFTC found that the indirect investment in Treasuries via a Treasury-only money market mutual fund “is essentially the risk equivalent of a direct investment” in Treasuries.

A similar position has been taken by other regulators. For example, the Comptroller of the Currency permits national banks to purchase for their own accounts shares of mutual funds provided the portfolios of such mutual funds consist solely of securities that a national bank may purchase directly. The Board of Governors of the Federal Reserve permits state member banks to purchase shares of mutual funds whose portfolios consist solely of securities that the state member bank may purchase directly.

- **The CFTC determined that the events of September 2008 are not an impediment to the use of money market mutual funds.**

The CFTC's analysis acknowledges the Reserve Fund crisis, noting that the "recent financial crisis" exposed the risks attendant to money market mutual funds and, in particular, their susceptibility to runs. The CFTC recognized that in response, the SEC amended Rule 2a-7 to address the risks inherent in money market mutual funds, which are aimed at reducing the perceived credit and liquidity risks of the money market mutual funds' underlying portfolios. Although acknowledging that the Rule 2a-7 enhanced restrictions could not rule out future runs on money market mutual funds, the CFTC believes that investments in large⁴ money market mutual funds will ensure that customer segregated funds are well diversified and in funds which are better positioned to withstand unexpected redemption requests.

To assure adequate portfolio diversification, the CFTC's amendment contains issuer-based limitations, including limitations of investing in small money market mutual funds, to protect FCMs from runs on particular funds and families of funds and ensure that money market mutual funds invested heavily by FCMs are large enough to handle a high volume of redemption requests while still allowing investments in small money market mutual funds. The CFTC's believes that the portfolio diversification requirements set forth by the CFTC amendments will provide greater security for customer funds, and ultimately to the FCMs that rely on those funds.

Conclusion

The CFTC has conducted a complete review and analysis concerning whether money market mutual funds are an appropriate investment for customers segregated funds and has

⁴ A "large" money market mutual fund is one that has a minimum of \$1 billion of assets and whose manager manages a minimum of \$25 billion of asset.

concluded that investment of customer funds in U.S. government money market mutual funds is “consistent with the objectives of preserving principal and maintaining liquidity.”

- The CFTC’s analysis endorses the SEC’s Rule 2a-7 amendments to money market funds;
- The CFTC’s analysis acknowledges that use of money market funds provide operational efficiencies to FCMs;
- The CFTC’s analysis determines that money market funds are an appropriate proxy for the underlying security;
- The CFTC’s analysis addresses the Reserve Fund “breaking the buck” event as not an impediment to the use of money market funds.

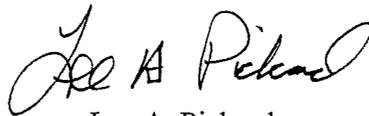
Each of the CFTC commissioners, including Chairman Gary Gensler, voted to adopt the amendments to permit FCMs to invest customer funds in money market mutual funds. This is notable, in that, Chairman Gensler is also a voting board member of the Financial Stability Oversight Council,⁵ established under the Dodd-Frank Act.

As we noted above, on more than one occasion, various members of the securities industry have requested the SEC to permit the use of U.S. government money market mutual funds as a qualified security for the investment of customer segregated cash. Given the identical purposes and obligations of the SEC’s Rule 15c3-3 and the CFTC’s Regulation 1.25, it is incumbent upon the SEC to follow the lead and the analysis of the CFTC and permit the use of U.S. Government money market mutual funds under Rule 15c3-3. Unlike the CFTC which has diligently analyzed the permitted investments for customer segregated funds, the SEC has yet to act on this matter.

⁵ The FSOC is responsible for comprehensive monitoring of our nation's financial system, charged with identifying threats to the financial stability of the United States; promoting market discipline; and responding to emerging risks to the stability of the United States financial system.

If you have any questions, please call Lee A. Pickard or Peter E. McLeod at
202.223.4418.

Sincerely,

A handwritten signature in black ink that reads "Lee A. Pickard". The signature is written in a cursive style with a large, stylized initial "L".

Lee A. Pickard

cc: Mr. Eugene F. Maloney, Executive Vice-President, Federated Investors, Inc.
Mr. John Ramsey, Deputy Director, Division of Trading and Markets
Mr. Thomas McGowan, Deputy Associate Director, Division of Trading and Markets.