John R. Jay, CFA
[redacted]

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

September 8, 2009

Re: Money Market Reform

Dear Madam Secretary:

In response to the request for comment on Money Market Reforms (File Number S7-11-09, ("Reform")), I believe that many of the reforms contained therein are insufficient to prevent systemic risk to the economy and are wholly unnecessary if amortized cost method of valuation ("$1 NAV") is used only for government and quasi-governmental securities. The original design and intent of the $1 NAV fund did not contemplate any credit risk. By including non-government backed securities the SEC fundamentally changed the nature of these funds resulting in some of the events of the past year.

Credit events on highly-rated, large corporations, such as those we have seen in the last 10 years, can be triggered quickly and by circumstances that cannot be foreseen, even weeks or months ahead. Quantitative models are highly unlikely to capture this risk, even as part of a stress test. Eventually, a major credit event will happen again in tier one investments and it will have a large systemic impact on the economy, as long as these funds take any credit risk beyond government risk. Internal stress testing will not prevent this. Only limiting the reaction in that event will reduce the risk to the economy.

The seizing of the credit markets after the Lehman Collapse was directly caused by the rational reaction of the money market mutual funds and their investors. Due to the artificial nature of the valuation, investors are incented to redeem immediately to avoid economic losses in the fund in a credit event and shift losses to those investors who do not redeem (or to the asset manager who supports the fund). Similarly, asset managers must retain as much as liquidity as possible, far beyond any cash reserves to handle the redemptions. They stop reinvesting cash flow. The net result of this behavior is a complete cessation of investing by the sector until confidence is restored.

MMMF became the nexus of U.S. finance through the purchase of commercial paper from corporations, asset backed commercial paper conduits and even variable rate demand obligations. These are the better examples of instruments that are financed through this system and provide a valuable service to economy. However, the availability of cash through the *artificial* benefits of $1 NAV valuation enabled such transactions to occur without an expectation of some loss on the part of investors.

Alternatively, in floating NAV funds, the investor sees minute, regular changes in value; an expectation of loss is created. In a stressed scenario, if the valuation was marked immediately, the investor has already taken the loss. He is not avoiding that real loss by pushing them onto other investors. Redemptions would be made to avoid prospective losses by the fund rather than those that have already occurred. Part of the reaction by investors is the fear from the extraordinary, which breaking the buck was and is.

By forcing credit financing into floating NAV funds, market forces will rationalize the size and extent that the short-term credit markets are used to finance; there is no market discipline where artificial accounting avoids transparency. There would be more scrutiny in the investments underlying the funds and should therefore lead to less abuse, such as investments in SIVs.

There would be changes to the money markets as a result of such a shift, as the most risk adverse population will use the remaining $1 NAV funds investing in government and quasi-government securities. The remaining investors will make decisions based on performance, including volatility of the NAV, rather than just net yield. They may reallocate to other forms of investing, depending on size, such as bank deposits and other insured products.

Part of the reform includes specific proposals and actions of liquidations under proposed rule 22e-3. In general these are sound concepts to avoid aggravating runs and providing time for orderly liquidation. However, as $1 NAV funds are a store of cash and needed liquidity for many individuals and companies, the loss of access for some investors is as troublesome as a capital loss. An alternative to the proposed liquidation would be for a new fund to be established immediately with the then liquid assets of the fund with each investor given a prorata ownership of the new fund at $1 NAV and in proportion to their ownership of the liquidated fund. This would enable investors to access a portion of their account, rather than having cash flow interrupted for one week, or longer as approved by the Commission. This might alleviate some of the liquidation pressures. Also, funds in that structure could use cash flow from maturities to redeem, possibly into the new fund at $1 NAV, rather than just staying the liquidations and forcing sales.

The remainder of the request for comments in the section, specifically, Temporary Suspension for Exigent Circumstances is a solid reminder that the Commission is propping up that which must inevitably fall. Any such failure that is not seen as anomalous will lead to the same systemic run that was seen after the Lehman bankruptcy.

As a citizen, I encourage the SEC to take this opportunity to encourage floating NAV funds for non-government risk. By virtue of the additional transparency, it should reduce reliance on short-term borrowing by the economy, something which to date has not received the attention warranted in academic circles. It will also mitigate the seizing of the credit markets when the next large credit default occurs, as investors are less economically incented to run on the funds.

Sincerely,

John R. Jay, CFA