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January 18, 2011

**VIA email (rule-comments@sec.gov)**

Ms. Elizabeth M. Murphy  
Office of the Secretary  
Securities and Exchange Commission  
100 F Street, N.E.  
Washington, D.C. 20549-1090

Re: File No. S7-37-10; RIN 3235-AK81 – Proposed Rulemaking Regarding Exemptions for Advisers to Venture Capital Funds, Private Fund Advisers With Less Than \$150 Million in Assets Under Management, and Foreign Private Advisers

Dear Ms. Murphy:

This letter presents the comments of Federated Investors, Inc. (“Federated”) on the Commission’s Proposed Rulemaking.<sup>1</sup> Federated and its subsidiaries manage approximately 90 money market funds with over \$330 billion in assets under management.

We support the Commission’s efforts to provide oversight under the Advisers Act of 1940 (the “Advisers Act”) with respect to the implementation of new exemptions from the registration requirements for investment advisers enacted as part of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the “Dodd-Frank Act”).<sup>2</sup> The Dodd-Frank Act, among other things, replaced the exemption contained in Section 203(b) with three new exemptions, one of which, Section 203(l), applies to an investment adviser that solely advises private venture capital funds. The Dodd-Frank Act directs the Commission to define the term “venture capital fund.”<sup>3</sup>

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<sup>1</sup> 75 Fed. Reg. 77190 (December 10, 2010) (the “Proposed Rule”).

<sup>2</sup> An investment adviser that is exempt from the SEC registration requirements, including investment advisers whose only clients are venture capital funds, may, nonetheless, be required to file certain periodic reports with the SEC.

<sup>3</sup> Section 407, Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. “(l) EXEMPTION OF VENTURE CAPITAL FUND ADVISERS.—No investment adviser that acts as an investment adviser solely to 1 or more venture capital funds shall be subject to the registration requirements of this title with respect to the provision of investment advice relating to a venture capital fund. Not later than 1 year after the date of enactment of this subsection, the

The Commission in its Proposed Rule proposes to define “venture capital fund” for purposes of the exemption, in part, as a fund that holds undeployed cash in “cash and cash equivalents, as defined in Section 270.2a51-1(b)(7)(i), and U.S. Treasuries with a remaining maturity of 60 days or less.”<sup>4</sup> A venture capital fund may hold cash from its investors until allocated to an investment opportunity; and subsequently, upon liquidation of the investment, which is then distributed to investors. The Proposed Rule proposes to define “cash and cash equivalents” by reference to Rule 2a51-1(b)(7)(i) under the Investment Company Act, which limits cash equivalents to “bank deposits, certificates of deposit, bankers acceptances and similar bank instruments.”

### **General Comment**

We are concerned that, as written, the Proposed Rule’s reference to Rule 2a51-1(b)(7)(i) in connection with “cash and cash equivalents” unnecessarily limits the types of cash instruments in which venture capital funds may hold undeployed cash. We respectfully request that the Commission specifically recognize that a venture capital fund may also hold cash in money market funds that are in compliance with all applicable requirements of SEC Rule 2a-7.

We believe that money market funds are widely recognized and utilized as cash equivalents, ranging, for example, from U.S. Generally Accepted Accounting Principles to banking regulations, for purposes of cash management and should be included as cash equivalents under the Proposed Rule. As money market funds are utilized for cash management purposes rather than a part of the venture capital fund’s investment activities, allowing such use would not frustrate the purpose of the investment adviser exemption or give rise to registration concerns.

### **Rule 2a51-1(b)(7)(i) omits important cash equivalents.**

The Proposed Rule’s reference to Rule 2a51-1(b)(7)(i) in connection with “cash and cash equivalents” unnecessarily limits the types of cash instruments in which venture capital funds may hold undeployed cash.

Rule 2a51-1(b)(7)(i) was promulgated in connection with determining whether an investor meets the definition of a “qualified purchaser” by examining whether such investor holds sufficient “investments” (generally securities and other assets held for investment purposes). Rule 2a51-1(b) provides a robust list of securities and other assets which when aggregated together determines whether an investor has sufficient

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Commission shall issue final rules to define the term ‘venture capital fund’ for purposes of this subsection. The Commission shall require such advisers to maintain such records and provide to the Commission such annual or other reports as the Commission determines necessary or appropriate in the public interest or for the protection of investors.”

<sup>4</sup> See Proposed Rule 203(l)-1(a)(2)(ii).

“investments” to be deemed a “qualified purchaser.” As such, Rule 2a51-1(b)(7)(i) does not purport to be a complete list of “cash equivalents.”<sup>5</sup> Indeed, the 1997 final release on Rule 2a51-1(b) indicates that money market funds may have been included as “cash equivalents” except that they were already included in the “securities” category of that rule.<sup>6</sup>

### **Money market funds are cash equivalents.**

Money market funds are mutual funds which are redeemable at any time without cost and carry a low amount of risk. They seek to generate income and preserve investor funds. They are stable and low-risk because they are required by law to, among other things, invest in highly liquid, low risk securities and meet stringent portfolio liquidity, credit quality, maturity, and diversification requirements.<sup>7</sup>

The Financial Accounting Standards Board (FASB), the highest authority in establishing generally accepted accounting principles for public and private companies, identifies money market funds as cash equivalents. The FASB defines cash equivalents as short-term, highly liquid investments that are readily convertible to known amounts of cash, and near their maturity that they present insignificant risk of changes in value because of changes in interest rates. According to FASB Codification 305-10-20, “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).”<sup>8</sup> (bold added)

The FASB Codification’s predecessor, FASB Statement of Financial Accounting Standards No. 95, similarly included money market funds as cash equivalents and additionally stated that, “Cash purchases and sales of those investments generally are part

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<sup>5</sup> The Rule Proposal recognizes that Rule 2a51-1(b)(7)(i) is not a complete list of cash equivalents as it does not include short-term U.S. Treasuries. The Commission proposes to explicitly include short-term U.S. Treasuries as a cash equivalent. See Proposed Rule, 75 Fed. Reg. at 77197. (“Furthermore, since rule 2a51-1 does not explicitly include short-term U.S. Treasuries, which we believe would be an appropriate form of cash equivalent for a venture capital fund to hold pending investment in a portfolio company or distribution to investors, our rule would include short-term U.S. Treasuries with a remaining maturity of 60 days or less among the investments a venture capital fund could hold.”)

<sup>6</sup> See Privately Offered Investment Companies, Final Rule, 62 Fed. Reg. 17512 n. 58 (Apr. 9, 1997). In a footnote to proposed Rule 2a51-1(b)(7)(i), the final release states that the cash and cash equivalent list does not include money market funds as they are securities which are already included under a different category of rule 2a51-1(b).

<sup>7</sup> See SEC Rule 2a-7, 17 C.F.R. § 270.2a-7.

<sup>8</sup> Definition of “Cash Equivalents” in paragraph 305-10-20 of the FASB Accounting Standards Codification.

of the enterprise's cash management activities rather than part of its operating, investing, and financial activities...."<sup>9</sup>

The Commission requires that financial reporting by publicly-traded companies adhere to these generally accepted accounting principles. Indeed, the Commission recently advised a publicly-traded company to review FASB Codification 305-10-20 in connection with identifying cash equivalents.<sup>10</sup> The Commission staff has also provided assurance in the past that money market funds shares may be treated as "cash items" for purpose of determining whether the issuer is an investment company, noting that many operating companies use money market funds as an alternative to bank checking accounts and other forms of short-term liquid investments and that the financial community generally views money market funds as the functional equivalent of the interest-bearing checking accounts offered by banks.<sup>11</sup>

Other financial regulators also recognize money market funds as cash equivalents. For example Federal Reserve Board Regulation T, concerning the regulation of credit to brokers and dealers, defines "cash equivalents" as "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.**"<sup>12</sup> (bold added).

The utilization of money market funds for cash management in the context of undeployed cash is widely recognized. It is an important option for cash management purposes. The recent regulatory reforms under SEC's Rule 2a-7 further enhance the safety of money market funds and underscore the usefulness of this option for undeployed cash.

**Including money market funds does not frustrate the proposed exemption.**

As noted above, the financial community generally views money market funds as the functional equivalent of the interest-bearing checking accounts offered by banks, and are utilized as part of an entity's cash management activities rather than part of its operating, investing, and financial activities. As cash management is not an investment function, there should be no concern that a firm managing a venture capital's cash, including the investment of cash in money market funds, should require SEC investment adviser registration.

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<sup>9</sup> FASB Statement of Financial Accounting Standards No. 95

<sup>10</sup> See SEC May 20, 2010 letter to Waters Corporation.

<sup>11</sup> See Willkie Farr & Gallagher No-Action Letter, 2000 SEC No-Act. LEXIS 916 (Oct. 23, 2000).

<sup>12</sup> See 12 CFR §220.2 (Credit by Brokers and Dealers).

In certain circumstances, the Commission has indicated that cash management, including the purchase and sale of money market funds, does not require investment adviser registration. Although not adopted, the Commission in its Proposed Interpretive Rule Under the Advisers Act Affecting Broker-Dealers,<sup>13</sup> advised that a broker-dealer which limits its activities to, among other things, having discretion to manage a client's cash holdings, e.g., exchanging a position in a money market fund for another money market fund, is not required to register with the SEC as an investment adviser.<sup>14</sup>

### **Federated's Proposal**

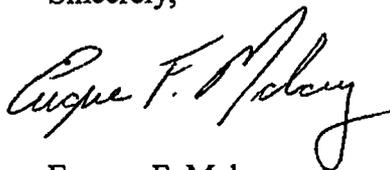
Based on the discussion above, Federated respectfully requests that the Commission revise proposed rule 203(l)-1(a)(2)(ii) to permit venture capital funds to utilize money market funds for undeployed cash as follows:

“Cash and cash equivalents, as defined in Section 270.2a51-1(b)(7)(i), *money market funds in compliance with Rule 2a-7 (17 CFR 270.2a-7)*, and U.S. Treasuries with a remaining maturity of 60 days or less.”

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Federated Investors, Inc. thanks you for this opportunity to comment on the Commission's Proposed Rulemaking.

Sincerely,



Eugene F. Maloney  
Executive Vice-President and  
Corporate Counsel

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<sup>13</sup> See Release No. IA-2652, 2007 SEC LEXIS 2229 (Sept. 24, 2007).

<sup>14</sup> Id.